No. 87——

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

KATHERINE JEAN GRAHAM, RICHARD M. HERMANN AND DAVID FORBES MAYNARD,
Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

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QUESTIONS PRESENTED

I. Whether the Commissioner of Internal Revenue incorrectly interpreted Section 170 of the Internal Revenue Code of 1954 in reversing seven decades of prior IRS policy and disallowing charitable contribution deductions for payments made by individual Scientologists solely to participate in religious services of their faith.

II. Whether denying charitable contribution deductions under Section 170 for payments by Scientologists to participate in their faith's core religious sacraments violates the religion clauses of the First Amendment.

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PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

Petitioners respectfully pray that a writ of certiorari issue to review the judgment and decree of the United States Court of Appeals for the Ninth Circuit in this case.

OPINIONS BELOW

The opinion of the court of appeals is reported at 822 F.2d 844 and is reprinted in the Appendix to this petition. 1a.[1] The order denying rehearing is not reported but is reprinted in the Appendix. 20a. The opinion of the United States Tax Court is reported at 83 T.C. 575 (1984) and is reprinted in the Appendix. 36a. The decisions of the Tax Court in each petitioner's case are also reprinted in the Appendix. 33a, 34a and 35a.

JURISDICTION

The judgment of the court of appeals (for which jurisdiction was invoked under 26 U.S.C. § 7482(a)) was entered on July 17, 1987. A petition for rehearing was denied on December 1, 1987. 20a. On February 19, 1988, Justice O'Connor extended the time within which to file this petition to and including March 30, 1988. 51a. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

The religion clauses of the First Amendment to the United States Constitution and pertinent portions of 26

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[1] References in this petition are indicated as follows:

To the numbered pages of the Appendix to this petition: (——a);

To the numbered pages of the Excerpts of Record filed with petitioners' main brief in the court below: (ER ——);

To the numbered pages of the trial transcript from the Tax Court: (Tr. ——).

U.S.C. § 170 and 26 U.S.C. § 501 are set forth in the Appendix to this petition. 48a.

STATEMENT OF THE CASE

The Nature of the Proceedings

Petitioner Katherine Jean Graham was denied an income tax deduction of $1,682.00 in payments for contributions to her church, the Church of Scientology, and was assessed a tax deficiency in the amount of $316.24 for the tax year 1972. ER 1-3. Petitioner Richard M. Hermann was denied a tax deduction of $3,922.00 for similar payments and was assessed a tax deficiency of $803.00 for 1975. ER 4-6. Petitioner David Forbes Maynard was denied a deduction for payments to the Church totalling $5,000.00 (including a carryover of $2,385.00 for contributions made in 1976) and was assessed a tax deficiency of $643.00 for 1977. ER 7-9.

The three taxpayers each challenged the Commissioner of Internal Revenue (the "Commissioner") for these tax deficiencies and the three cases were consolidated for trial in the Tax Court. At trial the petitioners and respondent entered into extensive stipulations of fact.[2]

The Tax Court upheld the Commissioner's disallowance of the contributions. 36a. Petitioners then appealed to the United States Court of Appeals for the Ninth Circuit, which affirmed the decisions of the Tax Court.

Appeals similar to petitioners' based on records incorporating the same factual stipulations have been decided by or are pending in all other United States Courts of Appeals except the appellate courts for the District of Columbia and the Federal Circuits.[3] Three other courts

[2] The stipulations filed in petitioner Graham's case (identical to the stipulations filed in the Hermann and Maynard cases except for certain individualized facts) are reprinted in the Appendix 22a.

[3] The Eleventh Circuit, however, has informed counsel that it intends to hold its case pending this Court's disposition of the petitions for writs of certiorari filed by both taxpayers and the government in related cases and, if any such writs are granted, pending the decision on the merits by this Court.

of appeals have issued opinions. Petitions for certiorari have been filed in each of these related cases, two on behalf of the taxpayers (also represented by the undersigned), *Hernandez v. Commissioner*, No. 87-963 and *Miller v. Commissioner*, No. 87-1449, and one on behalf of the Commissioner, *Commissioner v. Staples*, No. 87-1382. In both its petition in *Staples* and its brief in response in *Hernandez*, the government identified the instant case as the best case for this Court to consider the issues presented here and has stated that it does "not intend to oppose" the taxpayers' petition in this case. Pet. in No. 87-1382 at 9; Br. Resp. in No. 87-963 at 8.

Statement of Facts

The parties have stipulated that Scientology, the faith whose sacraments are at issue here, is a religion (31a, ¶ 52) and that the recipients of the contributions, the relevant Scientology missions and churches, were, at all relevant times, churches within the meaning of Internal Revenue Code § 170(b)(1)(A)(i) and tax-exempt religious organizations under § 501 of the Code eligible to receive contributions deductible under § 170. 31-31a, ¶ 53.

The payments at issue in this case are made for the core religious practice of the Church of Scientology known as "Auditing." Specifically, the record, through the detailed stipulations of fact, established that parishioners of Scientology are taught that "the individual is an immortal spirit who has a mind and a body" and "that the highest level of spiritual ability and awareness can be obtained only by progressing on a step-by-step basis through lower and intermediate levels of Auditing." 24a, ¶ 16. "Every Auditing session is structured and conducted in exact accordance with rituals, codes, doctrines and tenets of Scientology." 24a, ¶ 15. No subject matter is taught, studied or learned during auditing. 25a, ¶ 23. Dr. Thomas Love, a professor of religious studies at

California State University at Northridge, California, gave his uncontradicted expert opinion that "auditing," the service for which the bulk of contributions involved were made, is "the essential religious experience of the Church of Scientology." Tr. 291-295.

The Church of Scientology engages in another religious practice also at issue here known to Scientologists as "training." In training parishioners study "the doctrines, tenets, codes, policies and practices of Scientology" (25a, ¶ 24) and study the scriptures of Scientology to the exclusion of all other materials. Tr. 98, 111, 117-18. As part of training, a person may audit others. Tr. 111, 114. The purpose of undergoing training is to achieve religious enlightenment and the ability to help others (including the ability to audit another person). Dr. Love gave uncontradicted expert testimony that "training" is a form of religious observance, comparable to devotional study of sacred texts in the Buddhist and Judaic traditions. Tr. 313-17. Scientologists believe that the spiritual benefits and awareness derived from auditing and training accrue not only to the individual but also extend to the public at large. Tr. 103-05, 115, 130, 166-67, 179-82, 203, 208.

In accordance with those stipulations and testimony, the Tax Court found the practices at issue to be religious. 83 T.C. at 580, 42-43a ("Petitioners wanted to receive the benefit of various religious services provided by the Church of Scientology").

The Churches of Scientology have established charges for auditing and training and refer to the payments of such charges as "fixed donations" or "fixed contributions." 27a, ¶ 36. Such fixed donations are the payments at issue here. 28a, ¶ 40. Auditing is given in sessions. An "Intensive" is a specific number of hours—12½ or 25—of Auditing intended to be given over a short period of time. 25a, ¶ 21. Fixed donations are sometimes made for an Intensive of 12½ or 25 hours of Auditing. 27a, ¶ 37. These donations, which are based upon a religious

tenet of Scientology called the Doctrine of Exchange, constitute the source of most of the funds of the Churches of Scientology and are used to pay the costs of church operations and activities. 27-28a, ¶ 39. *See also* Tr. 136-39, 199-200.[4] Amounts of fixed donations have been set historically at levels that correspond roughly to a percentage of the income of church members. For example, the Tax Court found that 25 hours of auditing historically has been set at the equivalent of three months' pay for average middle-class church members. 83 T.C. at 578 n.7, 39a.

The taxpayers testified in Tax Court that they had made their payments so that they or their children could participate in religious services and because they wanted to support the religious goals and projects of their church. Tr. 166-67, 208-09, 260-61. None of the petitioners here received any material goods or secular services with respect to the payments at issue.

The government's position in this case is that payments by individuals to participate in the religious sacraments of their church may be disallowed depending on the form of such payment and the nature and value of the religious service provided. The Tax Court agreed and the Ninth Circuit affirmed.

The court of appeals held that payments to a church may not be deducted under § 170 of the Internal Reve-

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[4] The Doctrine of Exchange is based upon early writings of the founder of the Church of Scientology concerning the need to balance inflow and outflow (or, put another way, the need to give as well as receive). Tr. 136-37, 202-03. A person must outflow to maintain a balance and to be an ethical Scientologist. Tr. 202-03. A person who receives but does not contribute, or exchange something in kind will suffer spirtual decline. Tr. 136, 202-03. The Doctrine of Exchange operates in many personal realms of a Scientologist's life, including, for example, relationships and responsibilities with respect to one's children or community, in addition to providing the doctrinal basis for fixed donations. Tr. 202-03. The Tax Court found that the "Church of Scientology applies this doctrine by charging a 'fixed donation' for training and auditing." 83 T.C. at 577, 39a.

nue Code when such payments are made to receive religious services. The court concluded that participation in the religious sacraments of their Church constituted a "measurable, specific return" to the petitioners, a "quid pro quo" requiring disallowance of their deductions. 822 F.2d at 848-849, 8a. In reaching this determination, the court emphasized the "form" or "structure" of the transaction. *Id.* at 849, 850, 8a. The panel below also examined the Church's literature and concluded that "[i]f the Church's literature suggests that the [parishoner] is the direct and primary beneficiary of the [religious] services which are the fruits of his payments," the deductions were properly disallowed. *Id.* at 850, 11a. The court explicitly foreshadowed the potentially disruptive impact of its decision on the deductibility of payments to other churches. Referring to prior long-standing IRS revenue rulings and court decisions regarding analogous payments to other churches and synagogues, the court acknowledged: "we are not convinced that every one of those rulings would comport with the analysis of Section 170 that we have set forth here." *Id.* The court below further held that its construction of the statute did not violate the first amendment rights of the taxpayers, concluding that the government has a "compelling justification for its rule" that overcomes both the burden on the taxpayers' religious beliefs under the free exercise clause and the "disparate effect" of the government's application of the tax law in "treating Scientologists more harshly than other religions" contrary to the establishment clause. *Id.* at 853, 18a.

REASONS FOR GRANTING THE WRIT

I. THE DECISION OF THE COURT BELOW IS ONE OF EXCEPTIONAL IMPORTANCE AND CONFLICTS DIRECTLY WITH A DECISION OF THE EIGHTH CIRCUIT.

The court's decision below conflicts directly with the decision of the Eighth Circuit in *Staples v. Commissioner*, 821 F.2d 1324 (8th Cir. 1987). Indeed, it is difficult to imagine a squarer conflict since both of these

decisions reviewed the same Tax Court opinion and were based on the same record. The court below did not consider the *Staples* decision.

The Eighth Circuit held in *Staples* that the taxpayers' payments for religious services provided by the Church of Scientology were deductible. The court held that under IRS rulings, court opinions and the legislative history of § 170, the receipt of religious services is not the type of "material, financial or economic benefit" for which a deduction may be disallowed. The court observed that benefits from receipt of religious services are considered as a matter of law primarily to benefit the general public and only incidentally to benefit the individual participants. The court stated that:

> Religious observances of any faith are considered under the law of charity to be of spiritual benefit to the general public as well as to the members of the faith, with the private benefit to individual participants being merely incidental to the broader good that is served. . . . *The public benefit from religion remains and predominates regardless of whether church doctrines provide for traditional congregational worship or individual worship as in Scientology or whether donations are voluntary or fixed.*
>
> * * * * [R]egardless of the timing of the payment or details of the church's method of soliciting contributions from its members, an amount remitted to a qualified church with no return other than participation in strictly spiritual and doctrinal religious practices is a contribution within the meaning of section 170.

Id. at 1326-1327 (emphasis added).

Finally, the Eighth Circuit remarked upon the "incongruity of attempting to place a market value on religious participation" and noted the unprecedented nature of the proposals for valuation made by the First Circuit in the *Hernandez* case: "No case to which we have been cited values in that manner the strictly religious prac-

tices presented by the stipulations in this case." *Id.* at 1327. The practical and constitutional difficulties of attaching a value to a religious service led the Eighth Circuit in *Staples* to reject the government's position, concluding: "Spiritual gain to an individual church member cannot be valued by any measure known in the secular realm." *Id.* By reversing the Tax Court's decision, the *Staples* court found it unnecessary to reach the constitutional questions necessarily addressed by the appellate courts that have affirmed the Tax Court's holding.

In addition to presenting a direct conflict among the circuits, the issues raised by the decision below are of exceptional importance in the administration of the tax laws. First, unprecedented valuations of religious services for income tax purposes will be mandated; see Section IV, *infra*. Second, as discussed in detail in Section III, *infra*, the decision below grants the IRS a license to disallow deductions for payments by millions of Americans to their churches and synagogues. Third, the decision below represents a dramatic and unwarranted reversal of nearly seventy years of consistent IRS interpretations of § 170 to the contrary. *See* Section II, *infra*. Finally, the denial of deductions here violates the religion clauses of the first amendment. *See* Section V, *infra*.[5]

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[5] In addition to the direct conflict in the circuits over the deductibility under § 170 of the payments at issue here, the court below arrived at its decision only after adopting the position adverse to petitioners in a conflict within its own circuit over whether Tax Court decisions on appeal are to be accorded special deference on issues of law. The court below accepted without discussion (or even acknowledgement of the conflict) the view, expressed by the Ninth Circuit in *Magneson v. Commissioner*, 753 F 2d 1490, 1493 (9th Cir. 1985), that the Tax Court is entitled to special deference. 822 F.2d at 848, 7a. *Contra, Vukasovich v. Commissioner*, 790 F.2d 1409, 1411 (9th Cir. 1986). *See also, Schroeder v. Commissioner*, 831 F.2d 856, 858 (9th Cir. 1987) (following *Vukasovich* and refusing to follow *Magneson* and *Graham*, while noting: "Our case law conflicts on the question whether we should accord to the Tax Court special deference in deciding questions of law under the Internal Revenue Code.") The court below erred in granting special deference to the Tax Court on an issue of law.

In its brief in response to petitioner's request for certiorari in the *Hernandez* case, as well as in its own petition in the *Staples* case, the government agreed with petitioner that the Ninth Circuit decision here, along with two other courts of appeals decisions, *Hernandez v. Commissioner*, 819 F.2d 1212 (1st Cir. 1987), and *Miller v. Internal Revenue Service*, 829 F.2d 500 (4th Cir. 1987), "conflicts with the decision of the Eighth Circuit in *Staples v. Commissioner*, 821 F.2d 1324 (8th Cir. 1987)". Br. Resp. in No. 87-963 at 6; Pet. in No. 87-1382 at 6-7.

In addition, the government observed that if the "conflicting holdings" are permitted to stand "disparate tax treatment for similarly situated taxpayers" will result. Br. Resp. in No. 87-963 at 7; Pet. in No. 87-1382 at 6-7. The government also emphasized the important conflicts in the decisions in the courts of appeals on the "validity of the legal proposition" at issue here and in particular, over the applicability to religious services of this Court's holding in *United States v. American Bar Endowment*, 477 U.S. 105 (1986), which denied charitable contribution deductions for payments to purchase life insurance. Br. Resp. at 7; Pet. at 7. Accordingly, the government does "not oppose the petition" with respect to "the statutory question presented." Br. Resp. at 6. The government has suggested, however, that there is "no reason" for this Court to review the constitutional issues presented. Br. Resp. at 9. The significance of the constitutional issues raised by the decision below is discussed in Sections IV and V, *infra*. The relationship of the statutory and constitutional issue is also discussed in Section VI.

II. THE DECISION BELOW IMPROPERLY REVERSES NEARLY SEVEN DECADES OF CONSISTENT IRS PRACTICE.

For nearly 70 years, the Internal Revenue Service has allowed deductions as charitable contributions under § 170 for payments made by individuals to their churches and other religious organizations in order to participate in the religious sacraments of their faith. The form of making such payments has always, prior to the decision of the Tax Court below, been treated as irrelevant so long as the payment was for participation in religious practices. Payments for religious services have been granted deductibility by the IRS under § 170 even where the payment is fixed and/or required as a condition of receiving a religious service.

Beginning in 1919, shortly after the income tax was first enacted, the Internal Revenue Service has issued authoritative rulings and pronouncements that allow the deduction of payments for religious services regardless of the form in which the contribution is made. Accordingly, deductions have been allowed under § 170 even when receipt of religious services depends upon the payment of pew rentals, assessments or periodic dues (including tithes). *See* A.R.M. 2, 1 C.B. 150 (1919) (47a) ("In substance it is believed that these [along with 'basket collections'] are simply methods of contributing, although in form they may vary") and Rev. Rul. 70-47, 1970-1 C.B. 49 (*reaffirming* A.R.M. 2). *See also Staples*, 821 F.2d 1324, 1326; Rev. Rul. 76-323, 1976-2 C.B. 18; Rev. Rul. 71-580, 1971-2 C.B. 235.

The holding of the court below that an individual's receipt of a strictly religious benefit is a specific, measurable "quid pro quo" requiring denial of the charitable deduction is, therefore, a striking departure from the Internal Revenue Service's consistent interpretation of the tax law involving payments for religious services over the past nearly 70 years. As the court noted in *Staples v. Commissioner*, 821 F.2d 1324, 1326, "[n]either the tax

court nor the government has cited a case in which a taxpayer has been denied a deduction for payments keyed to participation in strictly religious practices."

The prior long-standing practice of the IRS is supported by the statute and its legislative history and advances the basic policies of the tax Code. Each of the prior cases denying charitable deductions to a qualified recipient has, until now, involved payments in exchange for goods or services provided in the secular or commercial marketplace. Thus, each can be understood as preventing tax-exempt organizations from providing taxpayers with secular goods or services paid for with tax deductible charitable contributions and thereby preventing such tax-exempt organizations from achieving an unfair competitive advantage over taxable providers of similar goods and services.[6] *See Staples*, 821 F.2d at 1327. In addition, such a policy is necessary to preclude deductible payments for secular goods and services that otherwise explicitly would be nondeductible under another provision of the Internal Revenue Code.

These sound tax policy reasons for disallowing charitable deductions to the extent that the payor receives valuable secular goods and services simply do not exist where, as here, strictly religious services are involved.

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[6] *See, e.g., United States v. American Bar Endowment*, 477 U.S. 105 (1986) (insurance); *Sedam v. United States*, 518 F.2d 242 (7th Cir. 1975) (admission to an old-age home); *Feistman v. Commissioner*, 30 T.C.M. (CCH) 590 (1971) (party following a bas mitzvah); *Murphy v. Commissioner*, 54 T.C. 249 (1970) (adoption services) (explicitly distinguishing the personal expense of adoption from a payment to participate in religious services). The Tax Court relied on only two cases, *DeJong v. Commissioner*, 309 F.2d 373 (9th Cir. 1962) and *Haak v. United States*, 451 F. Supp. 1087 (W.D. Mich. 1978), to support its conclusion that a payment for religious services was a *quid pro quo* that should disallow the deduction. Both cases involved payments made to a church school for the secular education of the taxpayers' children. *See also Winters v. Commissioner*, 468 F.2d 778 (2d Cir. 1972) and *Oppewal v. Commissioner*, 468 F.2d 1000 (1st Cir. 1972) (educational expenses).

Seven decades of consistent IRS interpretations allowing deductions for payments individuals have made to their religious organizations to participate in the religious sacraments of their faith—regardless of the form of the payment or the nature of the religious service provided in return—have rendered legislative amendments explicitly distinguishing religious services under § 170 unnecessary and have eliminated any need for persons of other faiths to litigate the issues raised by this appeal. Practitioners of all religious denominations heretofore have enjoyed religious services by making tax deductible payments. By disallowing deduction of Scientologists' payments for their religious services, the court below grants the IRS a license to challenge at will people's deductions for payments to participate in religious services and overthrows seven decades of IRS practice without any sound statutory or policy basis.

III. THE DECISION BELOW GRANTS THE IRS A LICENSE SELECTIVELY TO DISALLOW INDIVIDUALS' DEDUCTIONS FOR PAYMENTS SOLELY TO PARTICIPATE IN THE RELIGIOUS SERVICES OF THEIR FAITH.

No principled basis exists for distinguishing the payments of Scientologists challenged by the IRS here from a wide variety of other payments to other churches. Instead, the holding of the court below provides the IRS with a license to challenge tax deductions for payments to their churches taken by millions of religious Americans. Each of the appellate courts that have reviewed the Tax Court opinion here have alluded to the potentially far-reaching implications of upholding the government's position, but none of the affirming courts has squarely faced the challenges to other religions implied by their decisions. *See Graham v. Commissioner*, 822 F.2d 844, 850, 11a, ("We are not convinced that [rulings and case law allowing deductions for payments to participate in religious services of other religions] would comport with the analysis of section 170 that we have set forth here."); *Hernandez v. Commissioner*, 819 F.2d 1212, 1227 ("[W]e

have some doubt as to the continuing validity of the presumption in Rev. Rul. 70-47, 170-1 C.B. 39 [sic], that pew rents and mandatory church dues are tax deductible gifts. . . ."); *Miller v. Internal Revenue Service*, 829 F.2d 500, 505 ("We have no reason to believe that the IRS will fail to apply the principles that *emerge from this litigation* in its treatment of other religious groups.") (emphasis added). The Eighth Circuit essentially agreed: "If the [Scientologists'] . . . payments were not contributions, then 'the passing of the collection plate in church would make the church service a commercial project.'" *Staples v. Commissioner*, 821 F.2d 1324, 1327, *quoting*, *Murdock v. Pennsylvania*, 319 U.S. 105, 111 (1943).

Scientology's religious services are, to be sure, provided on an individual basis rather than in the more traditional congregational fashion of most Western religions. Indeed, the Ninth Circuit opinion below indicated that Church literature suggesting that the individual "is the direct and primary beneficiary" of the religious practices that "are the fruits of his payments" renders the payments nondeductible. 822 F.2d at 850, 11a. Regardless of denomination, however, religious people expect substantial individual spiritual benefits to flow from participation in their religious sacraments. Such expectations have never precluded deduction of payments for religious services under § 170, nor should they here.[7]

Numerous churches proselytize by telling their members that they will derive personal benefits, in terms of jobs, health and solutions to personal problems, among other benefits, from contributing to the church. For example, Roman Catholics make gifts to their churches in the name of specific saints in order to secure benefits in the category for which that saint is the patron. *See, e.g.*, S. Wilson, *Saints and Their Churches* at 21 (Cambridge

[7] For discussion of the analogous Christian practice of "spiritual direction," as well as the "individual" religious practice of "confession," recognized across many religious traditions including Christianity and Jainism, *see* Pet. in No. 87-963 at 16.

University Press). Numerous Protestant denominations also emphasize in their literature the personal benefits to be obtained from their religious services. *See, e.g.*, O. Roberts, *Seed Faith Scriptures* (1972) and P. Cho, *Salvation, Health, Prosperity* (1987). Telling their parishioners that participation in religious sacraments will benefit the individual does not distinguish Scientology from other religious denominations.

Neither the Internal Revenue Code nor its policies permit a distinction between individual and congregational worship in determining the allowability of a deduction under § 170. *Cf.*, *Hernandez*, 819 F.2d at 1227 ("The IRS found significance in the fact that, unlike the collective worship services obtained in exchange for pew rents and . . . membership dues, auditing and training sessions are performed in private sessions.") Moreover, such a distinction between individual and congregational worship would advantage or disadvantage individuals based upon the religious tenets of their denomination in contravention of the first amendment of the United States Constitution. *See, e.g., Larson v. Valente*, 456 U.S. 228, 244 (1982) and Section V below.

Nor does the "fixed donation" form of the payment to the Scientology church accord any principled basis for distinguishing the payments at issue here from payments to religious organizations of other faiths. The decision of the panel below would reverse dramatically prior IRS and court rulings that the *form* of payments does not warrant disallowance of deductions for religious services or for other charitable contributions. The panel below makes clear the critical nature of the form of the transaction:

> If a transaction is structured in the *form* of a quid pro quo, . . . then the transaction does not qualify for the deduction under section 170. It is the structure of the transaction, and not the type of benefit received, that controls.

822 F.2d at 849, 8a (emphasis added). *See also, Id.* at 849-50, 8-9a, (emphasizing other aspects of the form of the transaction). *Contra, Staples*, 821 F.2d at 1327 (rejecting "form" as an important factor). Disallowance of deductions for payments for religious services because of the form of the payment finds no support in the Internal Revenue Code and contradicts the fundamental principle of tax adjudication that requires the substance, not the form of a transaction, to govern. *See e.g., United States v. Phellis*, 257 U.S. 156, 168 (1921) (treating the superiority of substance over form as a well-settled principle of tax adjudication). Since 1919, when the IRS first decided to allow deductions for fixed mandatory payments to participate in religious activities, the substance, not the "form" or "structure" of a transaction has been held to govern. *See* A.R.M. 2, 1 C.B. 150 (1919), 47a ("In *substance* it is believed that [the payment of pew rentals, assessments or periodic dues (including tithes) along with 'basket collections'] are simply methods of contributing, although in *form* they may vary") (emphasis added) and Rev. Rul. 70-47, 1970-1 C.B. 49 (reaffirming A.R.M. 2).

Comparison with the Mormon tithe may be useful. Mormons are required to tithe in accordance with the church's "worthiness" standards so that they personally will be admitted to the temple. *See Corporation of the Presiding Bishop of the Church of Jesus Christ of Latter-Day Saints v. Amos*, 107 S.Ct. 2862, 2865 n.4 (1987). Mormon temples play a "critical role" in Mormon life, for it is in these temples that the most important rituals are performed, such as marriage and baptisms of the living and the dead. While Mormons have worship chapels also, they cannot supplant or replace the temples. In order to gain admission to temples, Mormons must obtain "temple recommends." It is the standing law for membership that each Mormon "tithe," or contribute 10% of his income, to the church. This practice is enforced through the rigorous questioning of those seeking temple recommends. J. Heinerman & A. Shupe, *The Mor-*

mon Corporate Empire, 96-97, 102-03 (1985). See also, Church of Jesus Christ of Latter-Day Saints, *The Priesthood Manual* Part 4 at 275 (Independence, Mo.: Herald Publishing House) ("The presenting of one's tithing statement is an act of worship.") There is as much of a *quid pro quo* in the religious benefits of Mormons as for Scientologists.[8]

Likewise, admission to Jewish High Holy Day services is often restricted to ticket holders. *See, e.g.*, M. Sklare, "The Sociology of the American Synagogue" in J. Neusner (ed.), *Understanding American Judaism; Toward the Description of a Modern Religion* Vol. I, at 95-96 (Anti-Defamation League of B'nai B'rith KTAV Publications, N.Y., 1975), ("While daily services, Sabbath services, and festal services are open to all, the demand for seats on the High Holy Holidays is so large that admission is commonly restricted to ticket-holders. In some congregations tickets are distributed only to members while in other synagogues they are sold to the public, but at a higher price than the charge made to members.") The emphasis on the "form" or "structure" of the transaction by the court below means that deductibility of payments by Jewish taxpayers solely to participate in their religion's sacraments might well turn on the extent to which their congregation chooses annual membership dues or High Holy Day tickets as fundraising devices. *See also*, Tr. 320, 306, 332-33 (Expert testimony as to parallels among the ways more traditional churches raise funds and Scientology's system of scheduled fixed donations for certain religious services).

In substance, the church's practices here are not materially different from more traditional religious organizations' use of—and the Commissioner's allowance of deductions for—fixed payments on a periodic or annual basis. As the Eighth Circuit recognized, a fixed payment schedule simply may be a more effective means of fundraising for a church that predominately provides individual, rather than congregational, services. *Staples*, 821 F.2d at 1327-28. The Tax Court acknowledged that the fixed payment schedule had an historical grounding in its linkage to the income levels of the church community, as do other more traditional religious payment schedules like the tithe, and is based on church doctrine. 83 T.C. at 577, 578 n.7, 39a. Nevertheless the court below relied on the fixed schedule to find that the payments in this case were for a quid pro quo and therefore nondeductible. 822 F.2d at 849-850, 8-10a. This elevation of form over substance is an improper interpretation of § 170, one with great potential to be used selectively—indeed misused—by the IRS to disallow deductions for payments for religious sacraments of many Americans.

[8] In fact, the form of payment disallowed deduction by the Tax Court in *Murphy v. Commissioner*, 54 T.C. 249 (1970), a case disallowing deduction for payments to receive adoption services, was equivalent to a tithe, an amount equal to ten percent of the taxpayer's income. Unlike tithes by Mormons, however, the taxpayer in *Murphy* received secular, not religious services, and the *Murphy* court explicitly distinguished religious from secular services.

IV. THE DECISION BELOW MISREADS AND IMPROPERLY EXTENDS THE 1986 DECISION OF THIS COURT IN *UNITED STATES V. AMERICAN BAR ENDOWMENT* TO REQUIRE IRS VALUATION OF RELIGIOUS SERVICES—A TASK THAT IS BOTH IMPRACTICAL AND UNCONSTITUTIONAL.

The court below relied upon the opinion of this Court in *United States v. American Bar Endowment*, 477 U.S. 105 (1986). 822 F.2d at 849, 8a. Extension of *American Bar Endowment* to require disallowance of deductions for the purely religious services at issue here constitutes an important misapplication of that recent decision of this Court.

American Bar Endowment involved an organization (ABE) that conducted a "trade or business" unrelated to any charitable activity—the provision of insurance to its members. ABE was able to obtain insurance at substantially lower cost than the members could have obtained elsewhere. ABE gave charitable organizations the excess of the members' premium payments over the cost

of providing the insurance. The only question in the case arising under § 170 of the Code was whether the excess payment constituted a contribution or gift deductible by the members. This Court held that the payments exceeding ABE's costs were not deductible because the members had failed to demonstrate that they could have purchased comparable insurance policies elsewhere for less than the full amount that they paid. 477 U.S. at 118.

In *American Bar Endowment*, the payments were in exchange for receipt of a secular economic benefit: insurance services. The taxpayers claimed deduction for an alleged difference between the payment and the fair market value of the benefit received. Here no secular economic benefit was received at all, and the analysis of *American Bar Endowment* has no application. The petitioners here received in "return" not a commercial economic product like life insurance, but instead participation in religious worship, which has no calculable financial or economic value.

Nevertheless, the court below read *American Bar Endowment* to require a determination of the monetary value of religious services received in return for a parishioner's payments. 822 F.2d at 849, 8-9a. *See also, Hernandez* 819 F.2d at 1216-18; *Miller*, 829 F.2d at 503. The government's papers in the *Hernandez* case make it clear that valuation of religious services would be required if its interpretation of § 170 is accepted: "The taxpayer . . . must at a minimum demonstrate that he contributed money or property *in excess of the value of any benefit he received in return.*" Br. Resp. in No. 87-963 at 5, *quoting, United States v. American Bar Endowment*, 477 U.S. at 118. *Contra, Staples*, 821 F.2d at 1328.

An example demonstrates the far-reaching implications of the government's construction of § 170. Many religious organizations use special fees for fundraising. Jewish synagogues, for example, sometimes charge members special fees to participate in a Passover service and meal. *See*, J. Feldman, H. Fruhauf, and M. Schoen (eds.),

Temple Management Manual (N.Y. 1984) at 9-12. Assume that a synagogue, eligible to receive charitable contribution deductions under § 170, sets a fee of $200, based on the income levels of its membership, for participation in a Passover meal. Under prior IRS interpretations of § 170, any excess of the $200 over the *value of the meal* would be deductible as a charitable contribution. Under the interpretation of § 170 urged by the government here, if the IRS challenged the participants' deduction, the taxpayer would have the burden of establishing whether, and to what extent, the $200 payment exceeded the *value of the meal and of the religious sacrament of participating in the Passover service.*

The court below concluded not only that the value of the benefit received by Scientologists from participation in the religious sacraments of their faith are "measurable," but that their value could be determined "simply by looking at the amount of money that [petitioners] were willing to pay." 822 F.2d at 849-850, 10a. The court justified this conclusion by characterizing the payments as having occurred in a "market setting" and dismissing as "not significant" the fact that "the benefit may have had value only to religious adherents." *Id.* Such a conclusion was explicitly rejected by the Eighth Circuit in *Staples*:

> Furthermore, these stipulations foreclose any reliance on the Church of Scientology's fixed donations as representing the value of its essential religious practices. Under the stipulations the fixed donations are not market prices set to reap the profits of a commercial moneymaking venture; rather, the Church of Scientology is a bona fide church which selected fixed donations as its mechanism for raising funds from its members.

821 F.2d at 1327-28.

Valuation of services provided by a charitable organization as necessarily equal to the amount paid—as done by the court below—is contrary to IRS rulings and case

law. *See, e.g.*, Rev. Rul. 67-246, 1967-2 C.B. 104; *American Bar Endowment*, 477 U.S. 105, 118; *DeJong v. Commissioner*, 309 F.2d 373 (9th Cir. 1962) (disallowing $400 of $1,075 claimed as a deduction for educational benefits); and *Oppewal v. Commissioner*, 468 F.2d 1000 (1st Cir. 1972) (disallowing $640 of $900 claimed as a deduction for educational benefits). The taxpayer, the IRS and ultimately the courts must place a monetary value on the services provided so that, whenever a payment to a church is in excess of the determined value of the religious services received in exchange, the donor may deduct the excess amount.

However, when payments are made and religious services are received in return important first amendment problems arise that simply are not at stake when this legal standard is applied—as it always has been prior to this litigation—only to secular services. As a result, the fundamental issue of statutory interpretation at issue here—whether to apply the legal standard announced in the *American Bar Endowment* case to payments in exchange solely for participation in religious sacraments—cannot be separated from the special treatment of religion under the first amendment. The First Circuit, in one of the related cases recognized that important "constitutional difficulties," such as "the problem of excessive entanglement in the affairs of a religious institution," may arise where the valuation of religious sacraments is at issue. *Hernandez v. Commissioner*, 819 F.2d at 1218.[9]

[9] Notwithstanding the First Circuit court's recognition of the important constitutional problems that would result, that court nevertheless offered two methods for valuing religious services that would violate the establishment clause of the first amendment, *viz.* by looking either to: (1) "the prices set by providers of similar services," or (2) "the costs of providing the service." *Hernandez*, 819 F.2d at 1217. Both of these methods faces practical and constitutional obstacles.

The suggestion by the *Hernandez* court that religious services may be valued by reference to "the price set by providers of similar services," *Hernandez*, 819 F.2d at 1217, is unworkable as well as unconstitutional. In the case of religious services, there are no "similar services" whose prices may be ascertained. Not only are there no prices to which comparison can be made, but the very notion of comparing relative values of religious services would violate first amendment prohibitions on entanglement of church and state both through the valuation of religious services and the creation of denomination preferences. *See, Walz v. Tax Commissioner*, 397 U.S. 664, 674 (1970); *Larson v. Valente*, 456 U.S. 228, 234.

Finally, valuing services based on the "costs of providing the services," *Hernandez* 819 F.2d at 1217 also would create constitutional difficulties. To determine the cost of providing services will require deep intrusions into a church's finances and operations. Excessive and unconstitutional church-state entanglement would result from such inquiry.

The *Staples* court remarked upon the unprecedented nature of the proposals for valuation made by the First Circuit: "No case to which we have been cited values in that manner the strictly religious practices presented by the stipulations in this case." 821 F.2d at 1327. The practical and constitutional difficulties of attaching a value to a religious service led the Eighth Circuit in *Staples* to remark upon the "incongruity of attempting to place a market value on religious participation" and to reject the government's position, concluding: "Spiritual gain to an individual church member cannot be valued by any measure known in the secular realm." *Id.*

The consistent prior practices of the IRS and the courts, and the construction urged here by petitioners—that, regardless of their form, payments for religious services are deductible under § 170 and therefore religious benefits need not be valued—avoids first amendment problems and thus is constitutionally proper, if not mandated. Indeed, special concern for entanglement with churches seems to account for the sharp distinction in IRS policy, heretofore consistently followed, between allowing without question deductions for membership dues to churches and synagogues and reducing deductions for membership dues to secular organizations by the value of secular benefits made available to members. *Compare*

Rev. Rul. 70-47, 1970-1 C.B. 49 (*reaffirming* A.R.M. 2, 1 C.B. 150 (1919)) (allowing deduction for all membership dues paid to churches and synagogues without inquiring into the value of benefits from such church memberships) *with* Rev. Rul. 68-432, 1968-2 C.B. 104 (detailing various instances where membership dues to secular charities are deductible only in part because the deduction is reduced by the value of secular benefits made available to members). Congress also has shown special consideration for religion and churches throughout the Internal Revenue Code in response to first amendment concerns. *See, e.g.*, 26 U.S.C. § 7611 (relating to restrictions on church tax inquiries and examinations).

V. THE INTERPRETATION AND APPLICATION OF SECTION 170 BY THE COURT BELOW VIOLATE THE RELIGION CLAUSES OF THE FIRST AMENDMENT.

The religion clauses of the first amendment are intended to provide comprehensive protection of religious liberty. They stand for the propositions that religious pluralism is essential to the welfare of the nation and that all citizens are entitled to protection from the imposition of an orthodoxy formulated by the government. *See, e.g., Everson v. Board of Education*, 330 U.S. 1, 8-14 (1947). Broadly speaking, the free exercise clause protects individuals from government interference with their religious beliefs and practices. The establishment clause prohibits governmental support for, control over, or inhibition of religious institutions and decisions.

In this case, the government's actions implicate both clauses. First, by taxing the plaintiff's primary religious practice—which is comparable to practices of other faiths for which the IRS has allowed deductions—the government has stated in effect that Scientology fails to satisfy the state's measure of orthodoxy. Second, by applying § 170 to allow deductions for payments for congregational worship regardless of the form of payment,

but not for the individual worship of Scientologists, the court below creates a denominational preference in violation of the establishment clause. *Larson v. Valente*, 456 U.S. 228, 244. Further, the decision below impermissibly entangles government with religion: the court's interpretation of § 170 requires valuation of purely spiritual matters. *See, Walz v. Tax Commission*, 397 U.S. 664, 669 (1970) and Section IV, *supra*.

The court below maintained that periodic payments required by churches of other denominations, such as pew rentals, and periodic dues (including tithes), are permitted to be deducted under § 170 because the "primary motivation" of the payor "is *presumed* to be charitable." 822 F.2d at 850, 11a (emphasis added). The court, however, did not accord a similar presumption to Scientologists. In addition, the court distinguished Scientologists from parishioners of other churches on the ground that individual Scientologists are the "direct and primary beneficiary" of their religious sacraments, whereas the public is considered to be the "primary beneficiary" of the religious sacraments of other religions. *Id.* The court reached this latter conclusion by looking to a publication of the Scientology Church that made the unremarkable statement, which might have been made by virtually any religious denomination, that "[t]he benefits obtainable from Church services . . . are personal and are experienced by the individual himself or herself." *Id.* The court's application of § 170 therefore allows the IRS to permit or disallow deductions for payments individuals make to participate in religious services based upon either the nature of the religious services or the content of representations made by the religious organization to its members.

Such distinctions among religions violate the nondiscrimination principles of the establishment clause. *Larson v. Valente*, 456 U.S. 228 (1982). Allowing the Internal Revenue Service to allow or deny deductions based upon the nature of religious services or church

representations authorizes it to impose a state-approved religious orthodoxy. *United States v. Ballard*, 322 U.S. 78 (1944). Surely neither purported differences in the nature of religious services nor representations made by churches to their members constitute a compelling governmental interest for treating religious denominations differently for tax purposes. *Larson v. Valente*, 456 U.S. at 247.

Government scrutiny of the representations churches make about the "personal" benefits to their parishioners of their religious services as occurred in the court below, also constitutes excessive church-state entanglement. The decision below would permit IRS to find that religious benefits constitute a quid pro quo requiring disallowance of deductions under § 170 whenever "the church literature *suggests* that the [church member] is the direct and primary beneficiary of the [religious] services." 822 F.2d at 850, 11a (emphasis added). A grant to IRS of such discretion invites that agency to discriminate among religious denominations. Such scrutiny also violates the prohibition on excessive intrusion into the internal affairs of churches.

The court of appeals' interpretation of § 170 also imposes an impermissible burden upon the free exercise of religion. *See Hobbie v. Unemployment Appeals Commission*, 107 S.Ct. 1046, 1048-50 (1987); *Thomas v. Review Board*, 450 U.S. 707, 716 (1981). As the stipulations recognize, Scientologists practice their core religious sacrament of "auditing" in a "personal" setting, because the scriptures of the religion required it to be conducted in that manner.[10] Disallowing deductions for payments for these services because they are provided in a "personal" rather than a congregational setting places a heavy burden on the central practice of the Scientology religion. The Tax Court also found that the "fixed donation" method used by the Church of Scientology for raising funds from its members was the Church's method of implementing a sincerely held religious belief, the Doctrine of Exchange. 83 T.C. at 577, 39a. *See also*, n. 4, *supra*. If petitioners and their Church were to abandon their scripturally mandated one-to-one religious services in favor of congregational services and their religiously based method of fundraising in favor of dues or tithes, petitioners would not experience disallowance of deductions for payments they make solely to participate in the religious sacraments of their faith. The first amendment, however, prohibits the government from imposing such pressure to abandon the tenets of one's religion; the application of § 170 by the court below is constitutionally prohibited. *See Hobbie v. Unemployment Appeals Commission*, 107 S.Ct. at 1048-49 and cases cited therein.

[10] "Auditing is generally conducted in a private session one to one, between the Auditor and the person being Audited. Every Auditing session is structured and conducted in exact accordance with the rituals, codes, doctrines and tenets of Scientology." ¶¶ 14, 15, 24a.

The government's disallowance of charitable contribution deductions imposes a burden on the taxpayer's religious practices by subjecting them to income tax. *See Bob Jones University v. United States*, 461 U.S. 574, 603-04 (1983). Once such a burden has been shown, the government must demonstrate a compelling state interest for its actions. *Id.* at 604. The court below failed to apply this doctrine. First, it dismissed the notion that disallowance of tax deductions imposes a burden.[11] 822 F.2d at 851, 13a.

[11] The Tax Court also held that its construction of § 170 imposed no free exercise burden because "there is no constitutional right to a tax deduction," and, therefore, that appellants were not deprived of anything guaranteed to them by the Constitution. 83 T.C. at 581, 43a. The court's analysis is wrong. This Court has emphasized, in connection with religious freedom, that once a government benefit has been created, it is unconstitutional to condition entitlement to the benefit on surrender of the exercise of first amendment rights:

[Continued]

Second, the court below misapplied the relevant constitutional standards by mischaracterizing petitioners as seeking special tax concessions for payments to participate in the services of their religion. 822 F.2d 852-53, 16-17a. To the contrary, this case does not involve a request for exemption from taxation that members of other religions must pay. *See United States v. Lee*, 455 U.S. 252 (1982). Rather, this case involves taxpayers asking only to be treated the same as members of other religions have always been treated and to be granted deductions for payments to participate in the religious sacraments of their church.

Finally, the court below accepted the IRS's contention that its compelling interest in the need to maintain a sound and uniform tax system justified both any free exercise burden and violations of the establishment prohibition. 822 F.2d 850-53, 11-18a. *See also*, 83 T.C. at 583 44a. The petitioners do not question the government's interest in a sound tax system. *United States v. Lee*, 455 U.S. 252. But the government's action here achieves exactly the opposite: by denying these deductions the IRS creates unsound, discretionary, and unequal tax administration. The court below erred in accepting the government's assertion that the payments at issue here are distinguishable from payments to other churches, which apparently would remain deductible. Drawing such distinctions among religions coupled with the enormous problems of valuing religious services that will be required, surely is not "sound" tax administration. The holding of the court below that its interpretation and application of the statute is necessary to further the government's interest in a "neutral and enforceable taxation system" trivializes this Court's continued insistence that burdens on religious free exercise may be justified only where necessary to accomplish an overriding governmental interest "of the highest order." *Sherbert v. Verner*, 374 U.S. at 406.

[11] [Continued]

> It is too late in the day to doubt that the liberties of religion and expression may be infringed by the denial of or placing of conditions upon a benefit or privilege.

Sherbert v. Verner, 374 U.S. 398, 404 (1963). *See also, Bob Jones University v. United States*, 461 U.S. 574, 603-04 (1983).

The decisions of the court below and of the Tax Court permit IRS to satisfy the "compelling state interest" requirement of the first amendment simply by claiming that any interpretation of the law advances "sound tax administration." [12] This decision—if left unreviewed by this Court—will have the practical effect of exempting

[12] The court of appeals stated that to permit the petitioners their deductions would "[presage] the exemption of a great many others," present "administrative difficulties," and a "danger of manipulation." 822 F.2d at 853, 17a. In fact, a "great many others" routinely are allowed deuctions. Allowing similar deductions to Scientologists would merely place them on equal footing with religious members of other denominations, who are permitted to deduct the payments they are required to make in order to participate in the religious life of their churches. The court of appeals is silent as to what "administrative difficulties" would be presented by permitting the deductions here; the IRS would merely be required to apply to Scientologists the same "presumption" that it applies automatically to adherents of other religious faiths, that their motivation is deemed to be charitable, and that the public is the "primary beneficiary" of the religious services. Such a rule has not created administrative difficulties during the seven decades it has been followed. Indeed, "administrative difficulty" is *created* by the holding that the Service may, and presumably should, examine the literature of religious denominations to determine which religious practices should be regarded as providing "personal" benefits to participants.

The court of appeals also failed to explain what it meant by "the danger of manipulation." No manipulation is present in this case: the essential facts of religiosity were stipulated to by the IRS and found by the Tax Court. The possibility that others may falsely claim that they make payments for religious services cannot disqualify the payments here. The IRS has always exercised its power to look beyond assertions of religiosity and to deny exemption or deductibility where such claims are found to be bogus. *See, e.g., Parker v. Commissioner*, 365 F.2d 792 (8th Cir. 1966); *Western Catholic Church v. Commissioner*, 73 T.C. 196 (1979), *aff'd*, 631 F.2d 736 (1980).

the administration of the tax law from the need to comply with the most fundamental constitutional requirements.

The consistent IRS practice of allowing charitable deductions for payments for religious services, regardless of their form or of their nature or value, has been sound during the nearly 70 years since the publication of A.R.M. 2 in 1919. The long-standing administrative distinction between secular and religious services is well grounded in current and historical policies of the tax code and is a permissible accommodation of religion that has avoided excessive church-state entanglement for nearly seven decades. *See, Corporation of Presiding Bishops of the Church of Jesus Christ of Latter-Day Saints v. Amos*, 197 S.Ct. 2862.

VI. THE STATUTORY AND CONSTITUTIONAL ISSUES IN THIS CASE ARE INEXTRICABLY INTERTWINED; THE STATUTE MUST BE INTERPRETED IN LIGHT OF THE CONSTITUTION.

The government's Brief in Response to the taxpayer's petition in the *Hernandez* case suggested that, although the statutory issues merit review by this Court, certiorari should not be granted on the constitutional issues because there is no square conflict in the circuits on the constitutional questions. Br. Resp. in No. 87-963 at 8-9. The government's position should be rejected by this Court. The constitutional questions in this case are substantial and are inextricably intertwined with the statutory issues. The *Staples* court was responding to constitutional values when it rejected the government's assertion that it could value religious services for tax purposes. *Staples*, 821 F.2d at 1327. Consideration of the substantial constitutional claims by petitioners is necessary to the proper interpretation of the statute.

Indeed, the special constitutional status of religion requires reversal of the court of appeals' application of § 170 in this case. A court must not construe an act of Congress to violate the Constitution "if any other possible construction remains available." *NLRB v. Catholic Bishop of Chicago*, 440 U.S. 490, 500 (1979). Where a particular interpretation of a statute raises serious constitutional issues, a court should not attribute that interpretation to Congress unless there is "present the affirmative intention of the Congress clearly expressed." *Id.*

In its effort to depict as unimportant petitioners' contentions regarding the establishment of a constitutionally prohibited denominational preference here, the government treats the very issue of statutory interpretation that is in controversy as if it had already been decided in the government's favor. Br. Resp. in No. 87-963 at 8-9. In claiming that its proposed interpretation of § 170 of the Internal Revenue Code is neutral across all religious denominations, the government simply asserts that the payments made by the petitioners here solely to participate in the core religious sacraments of their church do not fall within the Revenue Rulings that allow—without any question as to the nature or value of the religious services involved—deductions under § 170 for "pew rents, assessments, church dues *and the like*." Br. Resp. in No. 87-963 at 9, *citing*, A.R.M. 2, 1 C.B. 150 (1919) (updated and reaffirmed in Rev. Rul. 70-47, 1970-1 C.B. 39) (emphasis added). The applicability of that Revenue Ruling and its underlying policy of distinguishing religious from secular services under § 170, of course, is the very issue in this case. *See* Sections II-IV, *supra*. The Eighth Circuit in *Staples*, explicitly analogized the payments at issue here to the "passing of the collection plate in church," and found no important differences between this case and prior Revenue Rulings allowing deductions for payments to participate in religious services. 821 F.2d at 1326-28. The contention in the government's brief that there is no substantial constitutional issue in this case, therefore, is based entirely on the government's assumption of the validity of its interpretation of the very statutory question that is at issue here.

To the contrary, § 170 of the Internal Revenue Code should be interpreted to permit deduction for the payments by Scientologists to participate in their central religious practices, as well as deduction for the tithes, High Holy Day tickets, pew rents, dues and other fees required by churches and synagogues of other religious faiths. Such an interpretation is a constitutional accommodation to religion that avoids the far more substantial establishment and free exercise clause violations resulting from the application of § 170 by the court below.

CONCLUSION

For all the foregoing reasons, both of the questions presented in this petition for a writ of certiorari warrant plenary review by this Court. This petition for a writ of certiorari should be disposed of as appropriate in light of the pending petitions of certiorari in *Hernandez v. Commissioner*, No. 87-963, *Staples v. Commissioner*, No. 87-1382, and *Miller v. Commissioner*, No. 87-1449.

Respectfully submitted,

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March, 1988

APPENDICES

APPENDIX A

UNITED STATES COURT OF APPEALS
NINTH CIRCUIT

Nos. 84-7794, 84-7798 and 84-7799

KATHERINE JEAN GRAHAM,
Petitioner-Appellant,

v.

COMMISSIONER OF INTERNAL REVENUE SERVICE,
Respondent-Appellee.

RICHARD M. HERMANN,
Petitioner-Appellant,

v.

COMMISSIONER OF INTERNAL REVENUE SERVICE,
Respondent-Appellee.

DAVID FORBES MAYNARD,
Petitioner-Appellant,

v.

COMMISSIONER OF INTERNAL REVENUE SERVICE,
Respondent-Appellee.

Argued and Submitted Dec. 10, 1985

Decided July 17, 1987

Before WRIGHT, KENNEDY and BEEZER, Circuit Judges.

KENNEDY, Circuit Judge:

Taxpayers Katherine Jean Graham, Richard M. Hermann, and David Forbes Maynard appeal the Tax Court's decision upholding the determination of the Commissioner of Internal Revenue that they were not entitled to deduct certain payments made to the Church of Scientology, 83 T.C. 575. Appellants contend that they were entitled to the deductions under I.R.C. § 170 (1987), that denial of the deductions violates their rights under the free exercise and establishment clauses of the first amendment, U.S. Const. amend. I, and that the Commissioner has selectively enforced the tax laws against them in violation of their rights under the first and fifth amendments. U.S. Const. amends. I, V.

It has been conceded by the government, for purposes of this case, that the Church of Scientology is a religion entitled to receive deductible charitable contributions, and that its adherents are entitled to first amendment protections for the practice of Scientology. Some of the facts were stipulated to the Tax Court, along with numerous exhibits. The parties also stipulated to the entire record in a related case, *Church of Scientology of California v. Comm'r*, 83 T.C. 381 (1984). The historical or background facts are essentially uncontroverted on appeal, except for the relevance of certain matters. The Tax Court found that the payments in question were not charitable donations because of the motives and intent of the payors, and this ultimate factual finding is much contested on the appeal.

The First Circuit has issued an opinion in a case in which it considered the issues present in this case on a record identical to the one we review here. *Hernandez v. Comm'r*, 819 F.2d 1212 (1st Cir. 1987). Judge Coffin's opinion is thorough and insightful, and we reach the same conclusions as the First Circuit does, with some differences in emphasis and analytic approach. We affirm the Tax Court's decision.

The appellants are Scientologists and were so during the tax years in question. Scientology teaches that the individual is a spirtual being having a mind and a body. Part of the mind, called the reactive mind, is unconscious. It is filled with mental images that are frequently the source of irrational behavior. Through the administration of a Scientology process known as aduditing, an individual, called a preclear, is helped to erase his reactive mind and gain spirtual competence. Auditing is also referred to as processing, counseling, and pastoral counseling. Training, a Scientology discipline distinct from auditing, involves courses of instruction in the tenets of Scientology.

Scientologists believe that they can attain benefits from auditing and training, but only in degrees or steps. These include levels called Grades and higher levels called OT sections. The various steps or degrees of accomplishment are set forth in a chart entitled Classification Graduation and Awareness Chart of Levels and Certificates.

A trained Scientologist, known as an auditor, administers the auditing. He is aided by an electronic device called an E-meter. This device helps the auditor identify the preclear's areas of spirtual difficulty by measuring skin responses during a question and answer session. These auditing sessions are offered in fixed blocks of time called Intensives.

Training is also delivered to Scientologists by a trained Scientologist. Course offerings range from basic courses which introduce the doctrines and texts of Scientology through advanced courses which train and qualify auditors to deliver auditing at the higher level.

One of the tenets of Scientology is that any time a person receives something, he must pay something back. This is called the doctrine of exchange. The Church of Scientology applies this doctrine by charging a fixed

donation for training and auditing. With few exceptions, these services are never given for free. Thus, fixed donations are generally a prerequsite to a person's receiving auditing and training. These fixed donation payments constitute the majority of the Church of Scientology's funds and are used to pay the costs of Church operations and activities.

Over the period at issue, the general rates for the fixed donations for auditing varied with the amount of auditing time involved. The Church's price lists disclose that fees for auditing services ranged from $625 for a 12½ hour intensive to $4,250 for a $100-hour intensive, with additional fees for specialized types of auditing. Members of the Church of Scientology are encouraged to make advance payments for Scientology courses. If payment is made well in advance of the services to be rendered, a discount of 5 percent can be obtained by the member. When a Scientologist makes an advance payment, the Church credits his account. Once the individual begins receiving a service, his account is debited. It is the Church of Scientology's policy to refund advance payments upon request at any time before services are received.

The Church of Scientology promotes its services through free lectures, congresses, free personality tests, and handouts. Advertisements are placed in newspapers, magazines, and on the radio. These promotional activities are geared to be responsive to community concerns, which are determined from surveys.

The Tax Court found that the Church of Scientology operates in a commercial manner in providing these religious services. By internal policy memoranda, the Church sets the goal of making money, and it is an idea which permeates virtually all of the Church of Scientology's activities, its services, its pricing policies, its dissemination practices, and its management decisions.

In 1972 Graham made payments totaling $1,682 to the Church of Scientology, Hawaii, and to the Scientology and Dianetic Center of Hawaii. Of this amount, approximately $400 went toward training, and the balance went for auditing. Some of the payments toward courses were for Graham's daughters, Karen and Laurel. When Graham made those payments, she expected to receive, and did receive, the benefit of those services. On her 1972 income tax return, Graham deducted $1,682 as a charitable contribution.

In 1975 Hermann paid the Church of Scientology, American Saint Hill Organization, $4,875. At the time Hermann made these transfers, he expected to receive Class 0 to 9 training. Although Hermann did not take these courses, he did take other Scientology courses and has received auditing between 1974 and the present. On his 1975 income tax return, Hermann deducted $3,922 as a charitable contribution.

In 1977 Maynard paid the Church of Scientology, Mission of Riverside, $4,698.91 as advance payments for services. Although Maynard did not receive any services in 1977, he made these remittances with the expectation of taking Interiorization Processing, Expanded Dianetics, and auditing. On his 1977 income tax return, Maynard claimed a $5,000 charitable contribution deduction.

The Commissioner disallowed these claimed charitable contribution deductions, and the Tax Court upheld the Commissioner's decision. It held that the remittances to the Church of Scientology were not contributions or gifts within the requirements of section 170 because they "were not voluntary transfers without consideration, but were made with the expectation of receiving a commensurate benefit in return." *Graham v. Comm'r*, 83 T.C. 575, 581 (1984). The Tax Court rejected appellants' challenge under the free exercise clause, holding that "there is no constitutional right to a tax deduction," *id.*,

and that any burden on religion was justified by the "broad public interest in maintaining a sound tax system." *Id.* at 582 (quoting *United States v. Lee*, 455 U.S. 252, 260, 102 S.Ct. 1051, 1056, 71 L.Ed.2d 127 (1982)). The Tax Court also rejected appellants' claim under the establishment clause because the tests for determining deductibility under section 170 were based on secular criteria. *See id.*, 83 T.C. at 583. The Tax Court held that appellants' claim of selective discrimination was not supported by evidence of discriminatory action by the Commissioner or any of his agents.

We must determine first whether appellants' fixed donations qualify for the deduction granted by I.R.C. § 170. Section 170 grants a deduction for "charitable contributions" made within the taxable year. Section 170 (c) defines "charitable contribution" as "a contribution or gift to or for the use of" a variety of entities, among which are bodies that are "organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes . . . or for the prevention of cruelty to children or animals," provided that they meet certain other requirements. I.R.C. § 170(c)(2).

It has been stipulated for the purposes of this case that the Church of Scientology is a religion and an organization to which charitable contributions may be made under section 170. The statutory issue is whether or not appellants' payments qualified as contribution[s] or gift[s]."

The Tax Court, relying on *DeJong v. Comm'r*, 36 T.C. 896 (1961), *aff'd*, 309 F.2d 373 (9th Cir.1962), and *Haak v. United States*, 451 F.Supp. 1087 (W.D.Mich. 1978), held that appellants' fixed donations did not qualify for the deduction because they were not "voluntary transfers without consideration, but were made with the expectation of receiving a commensurate benefit in return," i.e. the transfer was a quid pro quo. 83 T.C. at

581. Appellants contend that the Tax Court applied an incorrect rule of law to their case by failing to focus on the nature of the benefits they received from the Church.

To the extent that an articulated legal standard is set out by the Tax Court as the basis for its decision, we will review that standard as a matter of law, while recognizing the special expertise of the Tax Court in deciding questions of law under the Internal Revenue Code. *Magneson v. Comm'r*, 753 F.2d 1490, 1493 (9th Cir.1985). The findings of the Tax Court disallowing claimed deductions will not be disturbed unless those findings are clearly erroneous. *See Kalgaard v. Comm'r*, 764 F.2d 1322, 1323 (9th Cir.1985).

We agree with the legal standards followed by the Tax Court in its decision, and we do not find its factual conclusions clearly erroneous. Implicit in the Tax Court's opinion is the recognition that the controlling question is not whether the payments in question were gifts for a religious purpose, but whether, consonant with the controlling rules and regulations, they were gifts at all.

The rule in this circuit is that a charitable gift or contribution must be a payment made for detached and disinterested motives. This formulation is designed to ensure that the payor's primary purpose is to assist the charity and not to secure some benefit personal to the payor. *See Babilonia v. Comm'r*, 681 F.2d 678, 679 (9th Cir.1982) (per curiam); *Allen v. United States*, 541 F.2d 786, 788 (9th Cir.1976); *Collman v. Comm'r*, 511 F.2d 1263, 1267 (9th Cir.1975); *Stubbs v. United States*, 428 F.2d 885, 887 (9th Cir.1970), *cert. denied*, 400 U.S. 1009, 91 S.Ct. 567, 27 L.Ed.2d 621 (1971); *DeJong v. Comm'r*, 309 F.2d 373, 376-79 (9th Cir.1962). Though it is true that the entire complex of a payor's motives often is not divorced from self-interest, *see Crosby Valve & Gage Co. v. Comm'r*, 380 F.2d 146, 146-47 (1st Cir. 1967), and that in the strictest sense a true charitable

purpose implies detriment to the donor, the law does not go so far. The test of detached and disinterested motive is designed to determine that no measurable, specific return comes to the payor as a quid pro quo for the donation. This focus on the external features of the transaction serves as an expedient for any more intrusive inquiry into the motives of the payor. *See id.* at 147; *Singer Co. v. United States*, 449 F.2d 413, 422 (Ct.Cl. 1971).

We think this is a proper approach and find it in full accord with the Supreme Court's recent opinion in *United States v. American Bar Endowment*, —— U.S. ——, 106 S.Ct. 2426, 91 L.Ed.2d 89 (1986). The Court held that "[t]he *sine qua non* of a charitable contribution is a transfer of money or property without adequate consideration." *Id.* at 2434. If the contributor expects a substantial benefit in return, then the contribution cannot be deducted. *Id.* at 2433; S.Rep. No. 1622, 83d Cong., 2d Sess. 196, *reprinted in* [1954] U.S. Code Cong. & Ad. News at 4629. If a transaction is structured in the form of a quid pro quo, where it is understood that the taxpayer's money will not pass to the charitable organization unless the taxpayer receives a specific benefit in return, and where the taxpayer cannot receive the benefit unless he pays the required price, than the transaction does not qualify for the deduction under section 170.

It is the structure of the transaction, and not the type of benefit received, that controls. Although we have often viewed the receipt of an economic benefit as sufficient to bar a section 170 deduction, *see Collman*, 511 F.2d at 1267; *Stubbs*, 428 F.2d at 887; *United States v. Transamerica Corp.*, 392 F.2d 522, 524 (9th Cir.1968), we have not held that the receipt of an economic benefit is the exclusive indicium of a nonqualifying transaction. *See Babilonia*, 681 F.2d at 679 (no reference to economic benefits); *DeJong*, 309 F.2d at 378 ("[w]here the payment is in return for services rendered, it is irrelevant

that the donor derives no economic benefit from it") (quoting *Comm'r v. Duberstein*, 363 U.S. 278, 285, 80 S.Ct. 1190, 1197, 4 L.Ed.2d 1218 (1960) (quoting *Robertson v. United States*, 343 U.S. 711, 714, 72 S.Ct. 994, 996, 96 L.Ed 1237 (1952))); *cf. Allen*, 541 F.2d at 788 (trial court found "no benefit, economic or otherwise"). Rewards or benefits to a payor can disqualify whether or not defined in economic terms. A donor will be found to lack a detached and disinterested motive for receipt of such noneconomic benefits as the right or privilege of adopting a child, *Murphy v. Comm'r*, 54 T.C. 249 (1970), or accompanying the child to provide guidance and companionship. *Babilonia*, 681 F.2d at 679. The test is not the economic character of what the payor receives but whether there is a specific, measurable quid pro quo for the donation in question. Though the economic aspect of a reward makes it easier to identify such a transaction, it is not a precondition to application of the test.

It is also the rule that the deductibility of a contribution does not depend on whether the benefits received in return are secular or religious. Section 170 authorizes deductions for contributions for charitable, scientific, literary, or educational purposes, and does not favor religious organizations over others entitled to benefit from taxpayers' deductible gifts or contributions. The statute cannot be read to permit religions to offer a deductible quid pro quo while other charitable organizations may not. *Hernandez*, 819 F.2d at 1217. It follows that the nature of a disqualifying quid pro quo does not depend on its secular or nonsecular character. The inquiry remains whether the donation is intended to benefit the charity without reference to a reciprocal and specific benefit to the donor, whether or not the benefit is religious. The taxpayers have not met that test here.

The Tax Court's ruling that appellants' fixed donations did not qualify for the deduction under the standards we

have discussed is a determination of fact, *see Babilonia*, 681 F.2d at 679; *Allen*, 541 F.2d at 788; *Collman*, 511 F.2d at 1267, and the evidence here is fully sufficient to sustain it. Solicitation for the services and agreements to render them based on price; conformity in price lists, and graduated prices based on the level of instruction; the contractual right to receive the service, and the right of refund if the service was not performed; account cards; and discounts for advance payments, all underscore that the payment matched, with some precision, the benefits to be received. That the benefit may have had value only to religious adherents is not significant, given its measurable attributes. The value of the quid pro quo received by the taxpayers was easy for the Tax Court to determine, simply by looking at the amount of money they were willing to pay for it in a market setting.

The record discloses that appellants looked upon their donations as payments made for the quid pro quo receipt of a definite number of hours of auditing or training. Appellant Graham stated that she "expected to get particular religious services in exchange" for her fixed donation. Appellant Hermann specifically noted the services for which he was paying on the checks that he sent to the Church. Appellant Maynard made his payments along with "Customer's Order" forms which itemized the payments as, for example, "100 hours @ $50.00/hr." Although appellants also stated that the payments were made out of a desire to help the Church or to support its goals, the Tax Court was not clearly erroneous in refusing to credit these statements. *See Sedam v. United States*, 518 F.2d 242, 245 (7th Cir. 1975) (stating that "[t]he taxpayer's intention governs, not his characterization of the payments").

We cannot accept appellants' contention that their payments must be deductible because they were made in connection with the performance of a religious service, the benefit of which inures directly to the public and

only indirectly to the person being audited. *See Murphy*, 54 T.C. at 253. As the enrollment form provided by the Church to new auditees states, "[t]he benefits obtainable from Church services . . . are personal and are experienced by the individual himself or herself." If the Church's literature suggests that the auditee is the direct and primary beneficiary of the auditing services which are the fruits of his payments, then the IRS was not clearly erroneous in making a similar finding. *See Estate of Wood v. Comm'r*, 39 T.C. 1, 6 (1962) (holding that transfer of stock in exchange for care of cemetery lot was noncharitable because trust agreement made "no provision for expenditure of income on the cemetery as a whole, but reserve[d] all the income for care of a private lot"). The Tax Court had sufficient evidence to distinguish appellants' fixed donations from deductible payments to religious organizations in which the primary motivation is presumed to be charitable, *see* Rev. Rul. 78-366, 1978-2 C.B. 241 (bequest for saying of mass); Rev. Rul. 70-47, 1970-1 C.B. 49 (pew rents, building fund assessments, and periodic dues); *see also Estate of Carroll v. Comm'r*, 38 T.C. 868 (1962) (expenditures to rebuild parish church situated on taxpayer's land), though we are not convinced that every one of those rulings would comport with the analysis of section 170 that we have set forth here.

Because we affirm the Tax Court's decision as to payments made for both auditing and training services, we need not discuss whether the payments made for training services were "in the nature of tuition." *DeJong*, 309 F.2d at 379.

We turn to the taxpayers' constitutional claims under the free exercise and establishment clauses of the first amendment. Our interpretation of section 170 is that payments for auditing sessions are not deductible because the payments are keyed to a specific, reciprocal benefit received by the taxpayers. The appellants' argument

seems to be that, as a result of the conflict between this interpretation of section 170 and Scientology's doctrine of exchange, a Scientologist can neither obtain the religious experience of auditing nor support the Church generally except through payments of after-tax dollars, though, by contrast, the adherents of other religions do not bear such disabilities. The taxpayers argue that a ruling which in effect limits their religion's support to after-tax dollars, and which conditions deductibility on abandonment of the doctrine of exchange, is a burden on the free exercise of their religion. The differential treatment, which favors other churches in receipt of donations, is alleged also to be a violation of the establishment clause. We rule against the taxpayers on these constitutional claims.

We first explain our free exercise analysis. To show a free exercise violation, the religious adherent, here the taxpayer, has the obligation to prove that a governmental regulatory mechanism burdens the adherent's practice of his or her religion by pressuring him or her to commit an act forbidden by the religion or by preventing him or her from engaging in conduct or having a religious experience which the faith mandates. *Hobbie v. Unemployment Appeals Comm'n of Florida*, —— U.S. ——, 107 S.Ct. 1046, 1049, 94 L.Ed.2d 190 (1987); *Sherbert v. Verner*, 374 U.S. 398, 404, 83 S.Ct. 1790, 1794, 10 L.Ed.2d 965 (1963). This interference must be more than an inconvenience; the burden must be substantial and an interference with a tenet or belief that is central to religious doctrine. *See Thomas v. Review Board*, 450 U.S. 707, 717-18, 101 S.Ct. 1425, 1431-32, 67 L.Ed.2d 624 (1981) (burden exists when state's regulation puts "substantial pressure on an adherent to modify his behavior and to violate his beliefs"); *Hernandez*, 819 F.2d at 1223; *Callahan v. Woods*, 736 F.2d 1269, 1273 (9th Cir.1984) (burden must be substantial, if indirect).

Denial of a tax deduction is not the most serious burden the government can create, for it does not prevent the observation of the adherent's religious tenets. *Bob Jones Univ. v. United States*, 461 U.S. 574, 603-04, 103 S.Ct. 2017, 2034-35, 76 L.Ed.2d 157 (1983); *see also Bown v. Roy*, —— U.S. ——, 106 S.Ct. 2147, 2153-54, 90 L.Ed.2d 735 (1986) (opinion of Chief Justice Burger) (discussing seriousness of burdens). Nevertheless, receipt of a tax deduction is a government benefit that must be dispensed within the bounds of the Constitution. *Regan v. Taxation With Representation of Washington*, 461 U.S. 540, 544-45, 103 S.Ct. 1997, 2000-01, 76 L.Ed.2d 129 (1983). If the taxpayers can show that the government conditions receipt of a tax deduction on abandonment of a central religious practice, this is a burden cognizable under the free exercise clause. *Sherbert*, 374 U.S. at 404, 83 S.Ct. at 1794. Measured by these standards, we doubt the taxpayers have shown a burden on the right of free exercise.

To begin with, the fact that taxpayers will have less money to pay to the Church, or that the Church will receive less money, does not rise to the level of a burden on appellants' ability to exercise their religious beliefs. Statutes are not invalid just because they affect a religious organization's operation. *EEOC v. Pacific Press Publishing Ass'n*, 676 F.2d 1272, 1279 (9th Cir.1982). Courts have uniformly rejected the notion that a reduction in potentially-available disposable income by denial of a deduction, without more, works a constitutionally-recognized hardship on activities protected by the first amendment. *See, e.g., Taxation With Representation*, 461 U.S. at 545-46, 103 S.Ct. at 2000-01; *Cammarano v. United States*, 358 U.S. 498, 513, 79 S.Ct. 524, 533, 3 L.Ed.2d 462 (1958); *Winters v. Comm'r*, 468 F.2d 778, 781 (2d Cir.1972). Any tax reduces the amount of money available to support the taxpayer's religion.

Nor does the perceived conflict between section 170 and the doctrine of exchange, as we understand that doctrine based on the briefs and the record, create a burden on taxpayers' religious beliefs. Although appellants' brief states that the doctrine of exchange derives from the need to balance "inflow" and "outflow," taxpayers Graham and Hermann both testified that the doctrine of exchange did not require the payment of money in return for training and processing. Record at 203, 231. If this were so, then the Church's requirement of payment in return for these services would not be a religious practice at all.

Further, the record does not indicate that an outright contribution to the Church would be refused by it or that a donor who gave without strings would be committing an act inconsistent with central precepts of Scientology. If we are correct in this, the Scientologists are not hurt by today's ruling: to the extent a Scientologist does not want to engage in a charitable transaction, he or she is free to pursue the doctrine of exchange that the law itself recognizes as being one of reciprocal benefit; and to the extent a Scientologist wishes to make a charitable contribution, he or she appears free to do so. Taxpayers are not put to the choice of abandoning the doctrine of exchange or losing the government benefit, for they may have both. They may practice the doctrine of exchange whenever they receive a quid pro quo benefit from the Church, and still deduct whatever contributions or gifts they make.

The statute does not impose a burden on the practice of auditing. Appellants need not forswear auditing services in order to make deductible payments, nor does the denial of the deduction create substantial pressure on them to abandon the practice of auditing. This was the essential rationale of the First Church in *Hernandez*, which also rejected taxpayers' arguments in the Scientology case. Taxpayers' situation is unlike the one in

Sherbert, where the individual could not be eligible for the government benefit unless she violated the precepts of her religion. Because appellants may receive the deduction without abandoning the practice of auditing, the fact that the government does not subsidize appellants' practice of auditing does not create a burden of the type recognized by *Sherbert*.

Though entertaining these doubts as to the validity of the taxpayers' positions, we do recognize that our own interpretation of the religion may be a disputed component of our reasoning. If so, further inquiry is warranted, for it is beyond our authority or our competence to give our own interpretation to religious principles. *United States v. Lee*, 455 U.S. 252, 257, 102 S.Ct. 1051, 1055, 71 L.Ed.2d 127 (1982). Though we feel bound to observe that the record for a free exercise burden is probably insufficient in this case, we nevertheless will accept for the remainder of our analysis the most favorable cast that can be put on the taxpayers' case. We will assume that a Scientologist may neither practice his or her religion nor support it without accepting reciprocal, quid pro quo benefits, and that as such charitable deductions are unavailable to the true believer in Scientology doctrine.

Even on this view of the case, however, we find no free exercise violation in the enforcement of the donative intent requirement of section 170. If the rules for the receipt of governmental benefits or exemption require a person to violate religious principles that are central to the particular faith, the government must accommodate the religious belief unless there is a compelling state objective for imposition of the rule in the particular case. This, as we understand it, is the holding of *Sherbert v. Verner*, 374 U.S. 406, 83 S.Ct. at 1795, as reaffirmed in *Hobbie v. Unemployment Appeals Comm'n of Florida*, 107 S.Ct. at 1049. We find that the government has met its burden on this issue.

The governmental interests at stake are the promotion of charitable gifts and contributions to certain organizations, and more generally, the maintenance of a sound and uniform tax system. All parties agree that these are interests of the highest order. The question is whether allowing appellants to deduct their fixed donations, even though they do not find within the requirements of section 170, would unduly interfere with the fulfillment of these important interests. *Lee*, 455 U.S. at 259, 102 S.Ct. at 1056.

It is hardly necessary for us to state that the charitable deduction need not be eliminated altogether, for that would defeat the objective of aiding education, science, literary pursuits, and religion, an end that has become a central feature of national tax policy. This takes us to the question of an exemption. To allow an exception for Scientologists is, we think, possible; but it is not feasible. An exemption would be fundamentally inconsistent with the elemental distinction between gifts and earned income and the concomitant congressional goal of encouraging gifts and contributions for eleemosynary purposes. *See, e.g.*, S.Rep. 1567, 75th Cong., 3d Sess., *reprinted at* 1939-1 C.B. part 2, at 779, 789 ("The committee believes that charitable gifts generally ought to be encouraged. . . ."). That factor again distinguishes this case from *Hobbie* and *Sherbert*, in which permitting sabbatarians to collect unemployment benefits was consistent with the objective of channeling those benefits to deserving recipients. Although we recognize that in some cases the government may not rely on its general interest in the underlying rule or program to overcome a claim for a religious exemption, *Callahan*, 736 F.2d at 1273, that principle is best applied where the underlying rule is not tied directly to the purpose of the program, as with the requirement of a social security number in the *Callahan* case. Where, as here, the purpose of granting the benefit is squarely at odds with the creation of

an exception, we think the government is entitled to point out that the creation of an exception does violence to the rationale on which the benefit is dispensed in the first instance.

We also find the government's interest in a neutral and enforceable taxation system is compelling, as that term has been interpreted in the context of taxation cases and the first amendment. In this regard, the controlling case is *United States v. Lee*, in which the Court held that the government's interest in mandatory participation in the social security system outweighed the burden that compliance imposed on the taxpayer's religious beliefs. 455 U.S. at 258-60, 102 S.Ct. at 1055-56. Significantly, the Court did not analyze the problem solely in terms of exempting the few adherents whose religious views were alleged to conflict with the law; rather, it stated that "it would be difficult to accommodate the comprehensive social security system with myriad exceptions flowing from a wide variety of religious beliefs." *Id.* at 259-60, 102 S.Ct. at 1056. In the taxation area, then, we are directed to view the cost of creating an exemption in a more general context than in other areas of governmental regulation.

We think the government's interest is incompatible with the creation of an exemption. The Internal Revenue Code is replete with exemptions and deductions that are triggered only when certain preconditions are met. As in *Lee*, the compelling state goal we have identified cannot be accomplished despite the exemption of a particular individual, *see Callahan*, 736 F.2d at 1272-73, because the soundness of the tax system depends on government's ability to apply the tax law in a uniform and evenhanded fashion, and the exemption of one presages the exemption of a great many others. The administrative difficulties in enforcing such a scheme, and the danger of manipulation, are manifest.

The taxpayers' establishment clause argument fails as well. Taxpayers argue that the rules of deductibility which we have announced will mean that their religion is inhibited, and uniquely so. This case is not one, however, in which the purpose of the government scheme is to visit a disability on a particular religion. The rules for charitable deduction are neutral in design and purpose. The precedent in *Larson v. Valente*, 456 U.S. 228, 102 S.Ct. 1673, 72 L.Ed.2d 33 (1982), relied upon by appellants, is inapplicable to this case, for there the law was not neutral in its design.

If we assume that the tax law, though neutral in its purpose, nevertheless has the effect of treating Scientologists more harshly than other religions, this disparate effect is not unconstitutional, for the reason that the government has a sufficient justification for its rule, in the context of tax law, as we have set forth. Denial of the deduction violates neither the free exercise clause nor the establishment clause of the first amendment.

Appellants claim that the government has selectively enforced its laws against them and not against other religious denominations. *See Nietmoko v. Maryland*, 340 U.S. 268, 71 S.Ct. 325, 95 L.Ed. 267 (1951); *Yick Wo v. Hopkins*, 118 U.S. 356, 6 S.Ct. 1064, 30 L.Ed. 220 (1886). This claim, however, is unsupported by evidence that the government discriminated against them in enforcing the tax laws. Their citation to internal IRS memoranda in support of their claim of selective enforcement is unavailing. Although the memoranda reveal some doubt about the proper tax treatment of appellants' fixed donations, they do not evidence the type of hostility to a target of law enforcement that would support a claim of selective enforcement. *See United States v. Ness*, 652 F.2d 890, 892 (9th Cir.) (per curiam) (requiring showing of impermissible motive), *cert. denied*, 454 U.S. 1126, 102 S.Ct. 976, 71 L.Ed.2d 113 (1981).

The decision of the Tax Court is AFFIRMED.

APPENDIX B

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

No. 84-7794 Tax No. 5837-76
No. 84-7798 Tax No. 9384-79
No. 84-7799 Tax No. 374-80

KATHERINE JEAN GRAHAM,
Petitioner-Appellant,

RICHARD M. HERMANN,
Petitioner-Appellant,

DAVID FORBES MAYNARD,
Petitioner-Appellant,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent-Appellee.

Upon Petition to Review a Decision of
The Tax Court of the United States

JUDGMENT

This Cause came on to be heard on the Transcript of the Record from The Tax Court of the United States, and was duly submitted.

On Consideration Whereof, it is now here ordered and adjudged by this Court, that the Decision of the said Tax Court of the United States in this Cause be, and hereby is AFFIRMED.

Filed and entered July 17, 1987.

APPENDIX C

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

No. 84-7794
Tax No. 5837-76

KATHERINE JEAN GRAHAM,
Petitioner-Appellant,

vs.

COMMISSIONER OF INTERNAL REVENUE SERVICE,
Respondent-Appellee.

No. 84-7798
Tax No. 9384-79

RICHARD M. HERMANN,
Petitioner-Appellant,

vs.

COMMISSIONER OF INTERNAL REVENUE SERVICE,
Respondent-Appellee.

No. 84-7799
Tax No. 374-80

DAVID FORBES MAYNARD,
Petitioner-Appellant,

vs.

COMMISSIONER OF INTERNAL REVENUE SERVICE,
Respondent-Appellee.

[Filed Dec. 1, 1987]

Appeal from a Decision of the
Tax Court of the United States

ORDER

Before: WRIGHT, KENNEDY, and BEEZER, *Circuit Judges.*

The panel as constituted in the above case has voted to deny the petition for rehearing. Judges Kennedy and Beezer have voted to reject the suggestion for a rehearing en banc, and Judge Wright recommends rejection of the suggestion for a rehearing en banc.

The full court has been advised of the suggestion for en banc hearing, and no judge of the court has requested a vote on the suggestion for rehearing en banc. Fed. R. App. P. 35(b).

The petition for rehearing is denied, and the suggestion for a rehearing en banc is rejected.

APPENDIX D

UNITED STATES TAX COURT

Docket No. 5837-76

KATHERINE JEAN GRAHAM,
Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

[Filed Dec. 6, 1982]

STIPULATION #1

In accordance with Tax Court Rule 91, the parties hereby stipulate the matters hereinafter stated, subject to the rights of the parties to introduce other and further evidence not inconsistent herewith and reserving to each of the parties the right to object to the materiality or relevance hereof in whole or in part.

1. Petitioner maintained her legal residence at 743 Pumehana, Hawaii, at the time of the filing of the petition herein.

2. Petitioner filed a timely Federal Income Tax return for the taxable year ending December 31, 1972, a true and correct copy of which is attached hereto and marked as Joint Exhibit 1-A.

3. Petitioner's income tax return for said taxable year was examined by respondent, who, on April 7, 1976, issued a notice of deficiency, a true and correct copy of which is attached hereto and marked as Joint Exhibit 2-B.

4. Petitioner claimed a charitable contribution deduction under I.R.C. § 170 for $2,379.50 transferred to the Church of Scientology of Hawaii and to the Scientology and Dianetic Center of Hawaii.

5. Each of Exhibits C through Q is a document received by petitioner from the Church of Scientology of Hawaii or from the Scientology and Dianetics Center for Hawaii, reflecting transactions of petitioner with one or the other of them.

6. During November of 1972, petitioner paid $200.00 to the Church of Scientology of Hawaii for Auditing, which payment is not reflected on respondent's Exhibits C through Q.

7. The neologisms "Scientology" and "Dianetics" were introduced by L. Ron Hubbard. Mr. Hubbard wrote *Dianetics: The Modern Science of Mental Health*, which was published in 1950 and which sets forth the general principles of Dianetics and Dianetic Auditing as discovered and developed to 1950.

8. Some of the beliefs and practices of Scientology are roughly described in lay terms in *Scientology, A World Religion Emerges in the Space Age*, a book copyrighted by L. Ron Hubbard. Respondent's Exhibit R attached hereto is a true copy of said book. Petitioner objects to said exhibit on grounds of relevance, hearsay and the first amendment.

9. The Church of Scientology of Hawaii is, and is considered by the Churches of Scientology to be, a church of the kind referred to by Scientologists as a "Class IV Church" or "Class IV Org." The Scientology and Dianetics Center of Hawaii is, and is considered by Churches

of Scientology to be, a church of the kind referred to by Scientologists as a "Mission."

10. There are many churches and missions in the United States and in other countries which practice, teach and promulgate Scientology. As used herein, "Churches of Scientology" refers collectively to such churches and missions, and "Scientologist" refers to members of such churches and missions.

11. The Churches of Scientology, including the Church of Scientology of Hawaii and the Scientology and Dianetics Center of Hawaii, follow common doctrines, practices and beliefs of Scientology.

12. The Churches of Scientology offer Auditing and courses to Scientologists.

13. Auditing, also variously referred to as "processing," "counselling" and "pastorial counselling," is conducted by a specially trained Scientologist, referred to as an "Auditor."

14. Auditing is generally conducted in a private session one to one, between the Auditor and the person being Audited.

15. Every Auditing session is structured and conducted in exact accordance with rituals, codes, doctrines and tenets of Scientology.

16. Scientologists are taught that the individual is an immortal spirit who has a mind and a body. Scientologists are also taught that the highest level of spiritual ability and awareness can be attained only by progressing on a step by step basis through lower and intermediate levels of Auditing.

17. The structure, ritual and content of each Auditing session are determined by the level of attainment of the Scientologist being Audited.

18. Some of the rituals used in Auditing include questions, commands and drills.

19. The Auditor acknowledges the response of the person being Audited, but offers no analysis of the response to the person being Audited.

20. An E-Meter is a device used in Auditing.

21. Auditing is delivered in sessions. An "Intensive" is a specific number of hours of Auditing intended to be given over a short period of time. An intensive is 12½ or 25 hours of Auditing and usually involves 12½ hours of Auditing.

22. An Auditor who conducts a session is expected to know and understand the rituals, codes, tenets and doctrines of Scientology applicable to the conduct of Auditing generally and to have mastered the particular material to be used in the session.

23. No subject matter is taught, studied or learned during an Auditing session (except that the Scientologist being Audited necessarily learns and understands the particular practice used in the session).

24. The Churches of Scientology offer courses to provide training in the doctrines, tenets, codes, policies and practices of Scientology and to train Scientologists as Auditors.

25. Training is delivered to Scientologists under the supervision of a trained Scientologist. Training is delivered in courses each of which includes specific material to be mastered by the students in order to complete the course. Courses range from basic courses which introduce the doctrines and tenets of Scientology through courses which train and qualify Auditors to deliver Auditing at the highest levels.

26. It is a doctrine of Scientology, and Scientologists are taught, that spiritual gains result from the study and understanding of the doctrines, codes and tenets of Scientology, whether or not the student receives Auditing.

27. Scientologists believe that they can attain benefits from Auditing, but only in degrees or steps. These include levels called "Grades" and higher levels called "OT Sections."

28. Respondent's Exhibit S attached hereto is a copy of a document headed "THE BRIDGE" which was published by the Church of Scientology of California. Petitioner objects to said exhibit on grounds of relevance, hearsay and the first amendment.

29. In contrast to Auditing, Auditor training and other courses furnished by the Churches of Scientology are instructional or educational; the student is expected to understand and learn the material which is the subject matter of the particular course he or she takes. As used herein, "course" means and refers to such services and not to Auditing. Some courses including Auditing by students and Auditing of students.

30. The Churches of Scientology deliver Auditing and training at various levels. A Scientologist who receives Auditing begins at the lowest level and progresses step by step to higher and higher levels. A Scientologist who receives training also begins at the lowest level and progresses step by step to higher and higher levels. Only Auditors who have been qualified by training at an appropriate level can deliver Auditing at that level.

31. Some of the Churches of Scientology also deliver administrator and executive training courses. The students in such courses are taught the management methods and policies of the Churches of Scientology, and are mostly staff members of the Churches of Scientology.

Such courses are occasionally taken by Scientologists who are not staff members. The subject matter of such courses includes Scientology doctrines, tenets and codes which are applicable to the administration and management of Scientology organizations.

32. The Churches of Scientology also deliver a few short courses of a general educational nature, designed to remedy educational deficiencies and to teach Scientology study methods, to enable the student to progress more rapidly in Scientology courses.

33. All of the courses offered by the Churches of Scientology are founded upon the doctrines and tenets of Scientology, in the manner of presenting the material studied and in the instructional methods.

34. The Scientology and Dianetic Center of Hawaii offers Auditing at Grades I through IV.

35. The Church of Scientology of Hawaii offer Auditing from Grade I through Grade IV and Auditor training from Class I through Class IV.

36. The Churches of Scientology have established charges for Auditing and for courses they deliver, and refer to payments of such charges as "fixed donations" or "fixed contributions." Such payments are hereinafter referred to as "fixed donations."

37. Fixed donations are sometimes made for an Intensive 12½ or 25 hours of Auditing.

38. Respondent's Exhibit T attached hereto is a copy of a schedule of fixed donations and book order form, copyrighted by L. Ron Hubbard and published by the Church of Scientology of California. Petitioner objects to said exhibit on grounds of relevance, hearsay and the first amendment.

39. Fixed donations constitute the source of most of the funds of the Churches of Scientology. Their only

other source of funds is from sales of Scientology literature, tapes of lectures by L. Ron Hubbard (the founder of Scientology) and artifacts.

40. The payments made by petitioner were fixed donations.

41. The Churches of Scientology do not actively solicit contributions from their members or from the public, other than fixed donations.

42. Petitioner first became a Scientologist in 1971 when she attended activities of the Scientology and Dianetics Center of Hawaii.

43. The Hubbard Qualified Scientologist Course (HQS) is an introductory course, one purpose of which is to familiarize the student with certain basic techniques used in Auditing.

44. Respondent's Exhibit U attached hereto is a copy of a pamphlet copyrighted by L. Ron Hubbard and published by the Church of Scientology of California. Petitioner objects to said exhibit on grounds of relevance, hearsay and the first amendment.

45. The Communications Course is an introductory course one purpose of which is to introduce those unfamiliar with Scientology to certain concepts of Scientology.

46. Respondent's Exhibit V attached hereto is a copy of a pamphlet copyrighted by L. Ron Hubbard and published by the Church of Scientology of California. Petitioner objects to said exhibit on grounds of relevance, hearsay and the first amendment.

47. The Communications Course referred to in respondent's Exhibit H was attended by petitioner's daughter, Karen.

48. The Communications Course referred to in respondent's Exhibit I was attended by petitioner's daughter, Laurel.

49. The Hubbard Qualified Scientologist Course referred to in respondent's Exhibit J was attended by petitioner's daughter, Karen.

50. The Hubbard Qualified Scientologist Course referred to in respondent's Exhibit K was attended by petitioner's daughter, Laurel.

51. Respondent's Exhibits W through AQ attached hereto are copies of documents, each of which was published and/or copyrighted as follows:

W Two page flyer, first page headed "Knowledge Services—Books," published by ASHO (Church of Scientology of California) and copyrighted by L. Ron Hubbard.

X Booklet entitled "Scientology & Dianetics," published by Church of Scientology of California.

Y Magazine, the cover of which is missing, published by the Founding Church of Scientology of Washington, D.C. and commencing with an article entitled "The Dangerous Environment."

Z Booklet entitled "Church of Scientology Information, Definitions, Rules," copyrighted by L. Ron Hubbard.

AA Flyer entitled "Gain Respect for Self and Others Through Scientology Training," published by the Los Angeles Organization (Church of Scientology of California) and copyright by L. Ron Hubbard.

AB Flyer entitled "Your Road to Total Freedom," published by Church of Scientology of California and copyrighted by L. Ron Hubbard.

AC Flyer commencing with excerpts titled "On Exchange," published by the San Francisco Organization (Church of Scientology of California) and copyright by L. Ron Hubbard.

AD Flyer entitled "Scientology Auditing gives you a chance to handle your environment better," published by The Church of Scientology Foundation (Church of Scientology of California) and copyright by L. Ron Hubbard.

AE Booklet entitled "Your Road to Clear Goes Through ASHO Foundation," published by Church of Scientology of California and copyrighted by L. Ron Hubbard.

AF Magazine entitled "Advance," Issue 18, published by the Advanced Organization (Church of Scientology of California) and copyright by L. Ron Hubbard.

AG Magazine entitled "Advance," Issue 19, published by the Advanced Organization (Church of Scientology of California) and copyright by L. Ron Hubbard.

AH Magazine entitled "Gateway," Issue 61, published by the Church of Scientology in San Francisco (Church of Scientology of California) and copyright by L. Ron Hubbard and copyright by L. Ron Hubbard.

AI Magazine entitled "Gateway," Issue 73, published by the Church of Scientology in San Francisco (Church of Scientology of California).

AJ Magazine entitled "THE AUDITOR: The Monthly Journal of Scientology," Issue 92 Worldwide, published by New American Saint Hill Organization (Church of Scientology of California) and copyright by L. Ron Hubbard and copyright by L. Ron Hubbard.

AK Magazine entitled "THE AUDITOR: The Monthly Journal of Scientology," Issue 91 Worldwide, published by New American Saint Hill Organization (Church of Scientology of California).

AL Magazine entitled "Cause," Issue 26, published by ASHO Foundation (Church of Scientology of California) and copyright by L. Ron Hubbard.

AM Magazine entitled "Cause," Issue 26, published by ASHO Foundation (Church of Scientology of California) and copyright by L. Ron Hubbard.

AN Magazine entitled "Clear News," Issue 107, published by AOLA (Advanced Organization, Los Angeles—Church of Scientology of California) and copyright by L. Ron Hubbard.

AO Magazine entitled "Clear News," Issue 104, published by AOLA (Advanced Organization, Los Angeles—Church of Scientology of California) and copyright by L. Ron Hubbard.

AP Magazine entitled "Realty," Major Issue 96, published by Church of Scientology of California and copyright by L. Ron Hubbard.

AQ Magazine entitled "Realty," Issue 102, published by Church of Scientology of California.

Petitioner objects to each of said exhibits on grounds of relevance, hearsay and the first amendment.

52. Respondent has not contested and will not contest, but only for the purposes of this litigation, petitioner's contention that Scientology was at all relevant times a religion.

53. Respondent has not contested and will not contest, but only for the purposes of this litigation, petitioner's contention that each Scientology organization to which petitioner paid money was at all relevant times a church within the meaning of I.R.C. § 170(b)(1)(A)(i), a corporation described in I.R.C. § 170(c)(2) and exempt

from general income taxation under I.R.C. § 501(a) as an organization described I.R.C. § 501(c)(3).

KENNETH W. GIDEON
Chief Counsel
Internal Revenue Service

By: /s/ Paul G. Wilson
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Date: 8/20/82

/s/ C. Cobb
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Date: 17 August 82

APPENDIX E

UNITED STATES TAX COURT
Washington, D.C. 20217

Docket No. 5837-76

KATHERINE JEAN GRAHAM,
Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

DECISION

Pursuant to the determination of this Court, as set forth in its Findings of Fact and Opinion filed October 15, 1984, it is

ORDERED and DECIDED that there is a deficiency due from the petitioner in her Federal income tax for the taxable year 1972 in the amount of $316.24.

/s/ Samuel B. Sterrett
Judge

Entered: Oct. 19, 1984

APPENDIX F

UNITED STATES TAX COURT
Washington, D.C. 20217

Docket No. 9384-79

RICHARD M. HERMANN,
Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

DECISION

Pursuant to the determination of this Court, as set forth in its Findings of Fact and Opinion filed October 15, 1984, it is

ORDERED and DECIDED that there is a deficiency due from the petitioner in his Federal income tax for the taxable year 1975 in the amount of $803.00.

/s/ Samuel B. Sterrett
Judge

Entered: Oct. 19, 1984

APPENDIX G

UNITED STATES TAX COURT
Washington, D.C. 20217

Docket No. 374-80

DAVID FORBES MAYNARD,
Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

DECISION

Pursuant to the Determination of this Court, as set forth in its Findings of Fact and Opinion filed October 15, 1984, it is

ORDERED and DECIDED that there is a deficiency due from the petitioner in his Federal income tax for the taxable year 1977 in the amount of $643.00.

/s/ Samuel B. Sterrett
Judge

Entered: Oct. 19, 1984

APPENDIX H

UNITED STATES TAX COURT

Docket Nos. 5837-76, 9384-79, 374-80

Filed October 15, 1984

KATHERINE JEAN GRAHAM, *et al.*,[1] *Petitioners*

v.

COMMISSIONER OF INTERNAL REVENUE, *Respondent*

Held: The payments made by petitioners to the various churches of Scientology were not charitable contributions within the meaning of sec. 170(c), I.R.C. 1954. The remittances were made with the exception of receiving a benefit, and such benefit was received. Thus, the transfers were in reality a quid pro quo. *Held, further*, denial of the claimed deductions did not violate any of petitioners' constitutional rights.

Robert N. Harris, Christopher Cobb, and *John E. Taussig,* for the petitioners.

James M. Kamman and *Charles Rumph,* for the respondent.

STERRETT, *Judge*: In these consolidated cases, respondent determined deficiencies in petitioners' Federal income taxes as follows:

Docket No.	*Petitioner*	*TYE Dec. 31—*	*deficiency*	*Date of Deficiency notice*
5837-76	Katherine Jean Graham [2]	1972	$316.24	Apr. 7, 1976
9384-79	Richard M. Hermann	1975	803.00	Apr. 4, 1979
374-80	David Forbes Maynard	1977	643.00	Nov. 14, 1979

[1] Cases of the following petitioners are consolidated herewith: Richard M. Hermann, docket No. 9384-79; David Forbes Maynard, docket No. 374-80.

[2] Petitioner Graham was unmarried during the tax year in question. Subsequently, she married, and her married name is Mrs. Elliott.

The issues before the Court are: (1) Whether payments made by petitioners to the various churches of Scientology [3] were deductible charitable contributions, and (2) whether denial of the claimed deductions would violate petitioners' constitutional rights.

FINDINGS OF FACT

Some of the facts have been stipulated and are so found. The stipulations of fact, together with the exhibits attached thereto, are incorporated herein by this reference. The parties specifically stipulated to the entire record in *Church of Scientology of California v. Commissioner*, 83 T.C. 381 (1984). All relevant findings of fact and court rulings from that case will be incorporated into this opinion. Since neither party argued to the contrary, it will be assumed that the Church of Scientology continued to operate at all relevant times in the same manner as it did in *Church of Scientology of California v. Commissioner, supra.*

For purposes of this litigation only, respondent did not contest petitioners' contentions that: (1) Scientology was at all relevant times a religion; (2) each Scientology organization to which petitioners paid money was at all relevant times a church within the meaning of section 170(b)(1)(A)(i),[4] and (3) Scientology was at all relevant times a corporation described in section 170(c)(2) and exempt from general taxation under section 501(a) as an organization described in section 501(c)(3).

Petitioners' residences at the time they filed their respective petitions in this case, and the places they filed

[3] For convenience, these various churches of Scientology will be referred to as either the Church of Scientology or the Church.

[4] Unless otherwise indicated, all section references are to the Internal Revenue Code of 1954 as amended and in effect during the taxable years in issue.

their timely income tax returns for their respective years are as follows:

Petitioner	*Residence*	*TYE Dec. 31—*	*Appropriate office of IRS*
Graham	Honolulu, HA	1972	Honolulu, HA
Hermann	Los Angeles, CA	1975	Fresno, CA
Maynard	Rialto, CA	1977	Fresno, CA

Petitioners were at all relevant times Scientologists. Scientology [5] teaches that the individual is a spiritual being having a mind and a body. Part of the mind, called the "reactive mind" is unconscious. It is filled with mental images that are frequently the source of irrational behavior. Through the administration of a Scientology process known as "auditing," an individual, called a "preclear," is helped to erase his reactive mind and gain spiritual competence. Auditing is also referred to as "processing," "counseling," and "pastoral counseling."

Scientologists believe that they can attain benefits from auditing and training, but only in degrees or steps. These include levels called "Grades" and higher levels called "OT sections." The various steps or degrees of accomplishment are set forth in a chart entitled "Classification Graduation and Awareness Chart of Levels and Certificates."

A trained Scientologist, known as an "auditor," administers the auditing. He is aided by an electronic device called an "E-meter." This device helps the auditor identify the preclear's areas of spiritual difficulty by measuring skin responses during a question and answer session. These auditing sessions are offered in fixed blocks of time called "Intensives."

One of the tenets of Scientology is that, anytime a person receives something, he must pay something back.

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[5] For an indepth review of the Scientology religion and its structure, see *Church of Scientology of California v. Commissioner*, 83 T.C. 381 (1984).

This is called the doctrine of exchange. The Church of Scientology applies this doctrine by charging a "fixed donation" for training and auditing. With few exceptions, these services are never given for free.[6] Thus, fixed donations are generally a prerequisite to a person's receiving auditing and training. These fixed donation payments constitute the majority of the Church of Scientology's funds, and are used to pay the costs of church operations and activities.

The general rates of the fixed donations for auditing in 1972 were as follows:

12½-Hour intensive	$ 625
25-Hour intensive	1,250
50-Hour intensive	2,350
75-Hour intensive	3,350
100-Hour intensive	[7]4,250

In addition, the Church of Scientology offered two specialized types of auditing for a higher fixed donation—

Integrity Processing	$750 per 12½-Hour intensive
Expanded Dianetics	$950 per 12½-Hour intensive

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[6] The Church of Scientology has a nine-volume encyclopedia of Scientology policy called the OEC series. Hubbard Communications Office Policy Letter (HCO PL) Sept. 27, 1970 (Issue I), 3 OEC 89, describes the Church of Scientology's policy against free services and price cutting. It states:

Price cuts are forbidden under any guise.

1. PROCESSING MAY NEVER BE GIVEN AWAY BY AN ORG. Processing is too expensive to deliver.

* * * *

9. ONLY FULLY CONTRACTED STAFF IS AWARDED FREE SERVICE, AND THIS IS DONE BY INVOICE AND LEGAL NOTE *WHICH BECOMES DUE AND PAYABLE IF THE CONTRACT IS BROKEN*. [Emphasis added.]

[7] Historically, the price of a 25-hour intensive was fixed at an amount equal to 3 months of pay for the average middle-class worker in the district of the Scientology Church providing the service.

Members of the Church of Scientology are encouraged to make advance payments for Scientology courses. If payment is made well in advance of the services to be rendered, a discount of 5 percent can be obtained by the member. When a parishioner makes an advance payment, the Church credits his account. Once the individual begins receiving a service, his account is debited. It is the Church of Scientology's policy to refund advance payments upon request at any time before services are received.[8]

The Church of Scientology operates in a commercial manner in providing these religious services. In fact, one of its articulated goals is to make money. This is expressed in HCO PL March 9, 1972, MS OEC 381, 384. It sets out the governing policy of the Church of Scientology's financial offices by exhorting these offices to "MAKE MONEY. * * * MAKE MONEY. * * * MAKE MORE MONEY. * * * MAKE OTHER PEOPLE PRODUCE SO AS TO MAKE MONEY." The goal of making money permeates virtually all of the Church of Scientology's activities—its services, its pricing policies, its dissemination practices, and its management decisions.

The Church of Scientology promotes its services through free lectures, congresses, free personality tests, and handouts. Advertisements are placed in newspapers, magazines, and on the radio. These promotional activities are geared to be responsive to community concerns, which are determined from surveys.

In 1972, Graham made payments totaling $1,682 to the Church of Scientology, Hawaii, and to the Scientology and Dianetic Center of Hawaii. Of this amount, approximately $400 went towards training, the balance went for auditing. These payments were for the Hubbard Qualified Scientologist course (HQS), Communications course, and auditing. Some of the payments toward courses were for Graham's daughters, Karen and Laurel. When Graham made those payments, she expected to receive, and did receive, the benefit of those services. On her 1972 income tax return, Graham deducted $1,682 as a charitable contribution.

[8] No evidence was produced with respect to the actual amounts, if any, of such refunds during the tax years in issue.

In 1975, Hermann paid the Church of Scientology, American Saint Hill Organization (ASHO) $4,875. At the time Hermann made these transfers, he expected to receive Class 0 to 9 training. While Hermann did not take these courses, he did take other Scientology courses and has received auditing between 1974 and the present. On his 1975 income tax return, Hermann deducted $3,922 as a charitable contribution.

In 1977, Maynard paid the Church of Scientology, Mission of Riverside, $4,698.91 as advance payments for services. While Maynard did not receive any services in 1977, he made those remittances with the expectation of taking Interiorization Processing, Expanded Dianetics, and auditing. On his 1977 income tax return, Maynard claimed a $5,000[9] charitable contribution deduction.

In the respective notices of deficiency, respondent disallowed these claimed charitable contribution deductions. Respondent maintains that it was not established that the payments to the Church of Scientology were contributions or gifts rather than payments for services or merchandise.

Issue 1. Deductibility of Payments Made

The taxpayer has the burden of proving that a particular payment is a "contribution or gift." *New Colonial Ice Co. v. Helvering*, 292 U.S. 435, 440 (1934); *Welsh v. Helvering*, 290 U.S. 111 (1933); Rule 142(a), Tax

[9] This amount consisted of a $2,385 carryover from 1976 transfers and $2,615 for transfers in 1977.

Court Rules of Practice and Procedure. Petitioners argue that their remittances to the Church of Scientology met the statutory requirements of section 170, subsections (a) and (c), and thus were deductible charitable contributions. Respondent maintains that those payments were not "contribution[s] or gift[s]" within the meaning of section 170(c). Rather, he insists they were made to purchase services, i.e., a quid pro quo, and thus were nondeductible personal expenditures.

Section 170(a)(1) allows as a deduction any charitable contribution payment which is made within the taxable year. Section 170(c) defines the term "charitable contribution" as "a contribution or gift." Neither section 170 nor the regulations further elaborate on the meaning of "charitable" contribution." This issue was addressed, however, in *DeJong v. Commissioner*, 36 T.C. 896 (1961), affd. 309 F.2d 373 (9th Cir. 1962). There, the Court stated—

> As used in this section the term "charitable contribution" is synonymous with the word "gift." * * * A gift is generally defined as a *voluntary transfer* of property by the owner to another *without consideration* therefore. If a payment proceeds primarily from the incentive of anticipated benefit of the payor beyond the satisfaction which flows from the performance of a generous act, it is not a gift. * * * [*DeJong v. Commissioner*, *supra* at 899. Citations omitted; emphasis added.]

Petitioners wanted to receive the benefit of various religious services provided by the Church of Scientology. The Church of Scientology, however, generally provided those services only if they were purchased. To encourage such purchases, the Church of Scientology gave a 5-percent discount to parishioners who made advance payments. A person who made an advance payment but chose not to receive the services could request a refund of

his money. Petitioners thus made payments to the Church in exchange for those services.

The record demonstrates clearly that these payments were not voluntary transfers without consideration, but were made with the expectation of receiving a commensurate benefit in return. In addition, where contributions are made with the expectation of receiving a benefit, and such benefit is received, the transfer is not a charitable contribution, but rather a quid pro quo. *Haak v. United States*, 451 F. Supp. 1087, 1090-1091 (W.D. Mich. 1978).

Petitioners Graham and Hermann made payments for which they received religious services. They received a perceived benefit from their transfers. Petitioner Maynard made advance payments to the Church of Scientology. While he did not receive any religious services in 1977, his account was credited for his remittances. This credit entitled him to receipt of services in the future. It was that entitlement which constituted his receipt of a perceived benefit, or the quid pro quo.

Accordingly, none of the payments petitioners made were charitable contributions within the meaning of section 170(c). Instead, they were nondeductible personal expenditures.

Issue 2. Constitutional Arguments

Petitioners maintain that denial of the deduction interferes with their constitutional right to the free exercise of their religion. It is well established that there is no constitutional right to a tax deduction. Benefits granted to taxpayers, such as deductions for charitable contributions, are matters of legislative grace. *Interstate Transit Lines v. Commissioner*, 319 U.S. 590, 593 (1943); *New Colonial Ice Co. v. Hervering*, *supra* at 440; *Winters v. Commissioner*, 468 F.2d 778, 781 (2d Cir. 1972), affg. a Memorandum Opinion of this Court. Further, denial of this deduction does not violate the free

exercise clause of the First Amendment. *Parker v. Commissioner*, 365 F.2d 792, 795 (8th Cir. 1966), cert. denied 385 U.S. 1026 (1967); *Winters v. Commissioner*, *supra* at 781. The constitutionality of the denial of this deduction was well stated by the Supreme Court in *Cammarano v. United States*, 358 U.S. 498, 513 (1959)—

> Petitioners are not being denied a tax deduction because they engage in constitutionally protected activities, but are simply being required to pay for those activities entirely out of their own pockets, as everyone else engaging in similar activities is required to do under the provisions of the Internal Revenue Code. * * *

Respondent is not precluding petitioners from engaging in constitutionally protected activities. Petitioners may practice their beliefs; they just will not be subsidized for them.

Even if denial of the deduction interfered with petitioners' practice of their religious beliefs, not all burdens on religion are unconstitutional. *United States v. Lee*, 455 U.S. 252, 257 (1982). See also, e.g., *Prince v. Massachusetts*, 321 U.S. 158, 163-166 (1944); *Reynolds v. United States*, 98 U.S. 145, 166-167 (1878). The limitation on religious liberty can be justified by showing that it is essential to accomplish an overriding governmental interest. *United States v. Lee*, *supra* at 257-258. The Supreme Court has stated that "Because the broad public interest in maintaining a sound tax system is of such a high order, religious belief in conflict with the payment of taxes affords no basis for resisting the tax." *United States v. Lee*, *supra* at 260.

Petitioners also argue that denial of the deductions violates the establishment clause of the First Amendment.[10] Their argument is twofold. First, disallowance

[10] Petitioners raised similar establishment clause arguments in *Church of Scientology of California v. Commissioner*, 83 T.C. at

would result in disparate treatment of petitioners, in violation of the neutrality requirement of the First Amendment. Second, disallowance would be the result of excessive Government entanglement with religion, in violation of the First Amendment.

Petitioners place heavy emphasis on *Larson v. Valente*, 456 U.S. 228 (1982). In that case, Minnesota had enacted a statute imposing registration and reporting requirements on religious groups which solicited more than 50 percent of their contributions from nonmembers. The Supreme Court held that the statute violated the establishment clause of the First Amendment. In so doing, they rejected an argument that the statute was facially neutral and found instead that it made "explicit and deliberate distinctions between different religious organizations." *Larson v. Valente*, *supra* at 247 n. 23. The Court further mentioned that "The fifty percent rule of section 309.515, subd. 1(b), effects the *selective* legislative imposition of burdens and advantages upon particular denominations." *Larson v. Valente*, *supra* at 253-254.

The instant case is distinguishable from *Larson* because section 70, unlike the charitable solicitation law in *Larson*, does not make classifications among religions. Furthermore, unlike *Larson*, here there is no legislative history revealing overt discrimination. Finally, even if section 170 has the effect of advancing one religion more than another, that fact alone does not make the statute unconstitutional. The establishment clause does not prohibit a statute from having a disparate impact on religious organizations provided the disparate impact results from the application of secular criteria. *Lynch v. Donnelly*, 465 U.S. ——, —— (1984); *Gillette v. United*

447-454. While that case dealt with the constitutionality of sec. 501(c)(3), its rationale is fully applicable to sec. 170 and we incorporate herein by this reference that portion of the opinion.

States, 401 U.S. 437, 452 (1971); *McGowan v. Maryland*, 366 U.S. 420, 442-444 (1961). Here the tests for determining the deductibility of claimed charitable contributions are based on secular criteria. Further, *Larson* is distinguishable from the case at bar because the section 170 classification bears equally upon all religious organizations. Thus, there is not the political divisiveness here that was prevalent in *Larson*. Accordingly, the argument of unconstitutionality under the establishment clause is rejected.

Finally, petitioners insist that denial of the claimed deductions was due to selective discriminatory action. They claim that their rights under the First Amendment and the equal protection component of the due process clause of the Fifth Amendment were violated. The evidence in this case does not demonstrate that any discriminatory action was taken against petitioners by respondent or any of his agents. Petitioners have failed to prove that violation of their rights occurred under either the First or Fifth Amendments.[11]

Decisions will be entered for the respondent.

[11] This issue of selective enforcement was also raised and rejected in *Church of Scientology of California v. Commissioner*, 83 T.C. at 453-454.

APPENDIX I

A.R.M. 2, 1 C.B. 150 (1919)

Section 214 (a) 11, Article 251: Charitable contributions.

The Committee is of the opinion that the distinction of pew rents, assessments, church dues, and the like from basket collections is hardly warranted by the act. The act reads "contributions" and "gifts." It is felt that all of these come within the two terms.

In substance it is believed that there are simply methods of contributing, although in form they may vary. Is a basket collection given involuntarily to be distinguished from an envelope system, the latter being regarded as "dues"? From a technical angle, the pew rents may be differentiated, but in practice the so-called "personal accommodation" they may afford is conjectural. It is believed that the real intent is to contribute and not to hire a seat or a pew for personal accommodation. In fact, basket contributors sometimes receive the same accommodation informally. On these grounds, the Committee is of the opinion that ordinarily and customarily pew rents, as well as so-called assessments and so-called dues, are to be regarded as contributions.

It is accordingly recommended that this interpretation be adopted.

APPENDIX J

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

First Amendment

Congress shall make no law respecting an establishment of religion, or prohibiting the free exercise thereof . . . .

Internal Revenue Code of 1954 (26 U.S.C.) § 170—Charitable, etc., Contributions and Gifts *

(a) Allowance of deduction.

(1) General rule. There shall be allowed as a deduction any charitable contribution (as defined in subsection (c)) payment of which is made within the taxable year. * * *

(b) Percentage limitations.

(1) Individuals.—In the case of an individual, the deduction in subsection (a) shall be limited as provided in the succeeding subparagraphs.

(A) General rule. Any charitable contribution to—

(i) a church or a convention or association of churches.

* * * *

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* Only those portions of 26 U.S.C. § 170 and 26 U.S.C. § 501 relevant to the discussion in this petition are set forth here. References to Title 26 United States Code are to the Internal Revenue Code of 1954, which was in effect when the tax returns at issue in this case and related cases were filed and when the Commissioner's notices of deficiency were issued. As part of the Tax Reform Act of 1986, the 1954 Code was redesignated the Internal Revenue Code of 1986. Pub. L. 99-514 § 2(a), 100 Stat. 2085, 2095. The portions of sections 170 and 501 of the 1954 Code pertinent to this case were not changed by the Tax Reform Act of 1986 and remain in force in identical form.

shall be allowed to the extent that the aggregate of such contributions does not exceed 50 percent of the taxpayer's contribution base for the taxable year.

(c) Charitable contribution defined. For purposes of this section, the term "charitable contribution" means a contribution or gift to or for the use of:

* * * *

(2) A corporation, trust, or community chest, fund, or foundation—

(A) created or organized in the United States or in any possession thereof, or under the law of the United States, any State, the District of Columbia, or any possession of the United States;

(B) organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes, or to foster national or international amateur sports competition (but only if no part of its activities involve the provision of athletic facilities or equipment), or for the prevention of cruelty to children or animals;

(C) no part of the net earnings of which inures to the benefit of any private shareholder or individual; and

(D) which is not disqualified for tax exemption under section 501(c)(3) by reason of attempting to influence legislation, and which does not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of any candidate for public office.

A contribution or gift by a corporation to a trust, chest, fund, or foundation shall be deductible by reason of this paragraph only if it is to be used within the United States or any of its possessions exclusively for purposes specified in subparagraph (B).

* * * *

Internal Revenue Code of 1954 (26 U.S.C.)
§ 501—Exemption From Tax on Corporations, Certain Trusts, Etc.

(a) Exemption From Taxation. An organization described in subsection (c) or (d) or section 401(a) shall be exempt from taxation under this subtitle unless such exemption is denied under section 502 or 503.

* * * *

(c) List of Exempt Organizations. The following organizations are referred to in subsection (a):

* * * *

(3) Corporations, and any community chest, fund, or foundation, organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purposes, or to foster national or international amateur sports competition (but only if no part of its activities involve the provision of athletic facilities or equipment), or for the prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private shareholder or individual, no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation, (except as otherwise provided in subsection (h)), and which does not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of any candidate for public office.

* * * *

APPENDIX K

SUPREME COURT OF THE UNITED STATES

No. A-640

KATHERINE JEAN GRAHAM, *et al.*,
Applicants,

v.

COMMISSIONER OF INTERNAL REVENUE

ORDER EXTENDING TIME TO FILE PETITION FOR WRIT OF CERTIORARI

UPON CONSIDERATION of the application of counsel for the applicants,

IT IS ORDERED that the time for filing a petition for writ of certiorari in the above-entitled cause be, and the same is hereby, extended to and including March 30, 1988.

/s/ Sandra D. O'Connor
Associate Justice of the Supreme
Court of the United States

Dated this 19th day of February, 1988.